

William Dudley

*State Predation in Ukraine: Local Agents and Property Rights Infringement after Euromaidan*

Non-exclusive (restricted) licence to reproduce thesis and make thesis public

I, William Dudley  
(author's name)  
(personal identification code: \_\_\_\_\_)

I. herewith grant the University of Tartu a free permit (non-exclusive licence) to:

1.1. reproduce, for the purpose of preservation and making thesis public, including for adding to the DSpace digital archives until the expiry of the term of copyright, and

1.2. make available to the public via the web environment of the University of Tartu, including via the DSpace digital archives, until the expiry of the term of copyright, my thesis  
e n t i t l e d

State Predation in Ukraine: Local Agents  
and Property Rights Infringement after  
Euromaidan'  
(title of thesis)

supervised by Adrian Florea  
(supervisor's name)

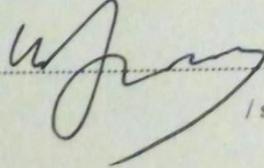
2. I am aware of the fact that the author retains the rights specified in p. 1.

3. I certify that granting the non-exclusive licence does not infringe other persons' intellectual property rights or rights arising from the personal data protection legislation.

Done at Tartu/Tallinn/Narva/Pärnu/Viljandi on \_\_\_\_\_ (date)

**Example of the author's declaration:**

I have written this Master's thesis independently. All viewpoints of other authors, literary sources and data from elsewhere used for writing this paper have been referenced.

  
.....  
/ signature of author /

The defence will take place on ..... / date / at ..... /  
time / ..... / address / in auditorium number ..... /  
number /

Opponent ..... / name / (..... / academic  
degree /), ..... / position /

# Introduction

## Summary of the Research Question and Main Findings

A recurring thesis of research into Ukraine's economic development since 1991 is that the failure of the Ukrainian state to introduce and enforce property rights for enterprises has held back economic growth and prosperity<sup>1</sup>. Much of the theoretical and empirical research on property rights security in Ukraine has focussed on the institutional development of the central state apparatus, to the neglect of how property rights are protected at the local level. It is assumed that legal and institutional constraints and reforms designed to strengthen property rights introduced at the central government level will strengthen property rights at the local level, but this has not been rigorously tested. To address this gap, my research draws upon a range of sources, including datasets from the Business Ombudsman of Ukraine, the Ukrainian State Regulatory Service, and a series of semi-structured interviews to explore an under-researched aspect of property rights security in Ukraine, "decentralized agent predation" i.e. *the threats posed to Ukrainian private enterprises' property rights by the predatory behaviour of local and regional authorities and other state agents*. I will explore the relationship between these threats and the constraints introduced to address them at the state principal level. The main findings of this research are as follows:

- (1) Constitutional constraints on the state principal's use of the tax administration system have had little impact on the opportunities for local actors in Ukraine's tax administration agencies to threaten the property rights of firms. Since 2014, reorganizing the State Fiscal Service on Oblast lines has minimized the presence of state agents at the local level and reduced the phenomenon of decentralized agent predation.
- (2) Local Regulatory Agencies and their discretionary powers to intervene in the local business environment to extract rents from businesses remain an important instrument through which local state agents are able to threaten firms' property rights, as indicated by data from the Business Ombudsman of Ukraine.

---

<sup>1</sup> E.g. Anders Åslund, "Will Ukraine be able to Establish Real Property Rights?", mBank – CASE Seminar Proceedings No 153/2017, *Centre for Social and Economic Research*, 2017 ([https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3130127](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3130127)), EU4Business, "Investing in SMEs in the Eastern Partnership, Country Report: Ukraine", June 2018, pg. 5 ([http://www.eu4business.eu/files/medias/country\\_report\\_2018\\_ua\\_def\\_lr\\_0.pdf](http://www.eu4business.eu/files/medias/country_report_2018_ua_def_lr_0.pdf)), Щорічна оцінка ділового клімату (ABCA, Annual Business Climate Assessment), USAID Leadership in Economic Governance Programme, 2017 (<https://www.slideshare.net/USAIDLEV/2016-2017-abcareportshort23042017final>)

- (3) Data from the State Regulatory Service combined with evidence from semi-structured interviews suggests that there is a lack of institutional pressure on local councils and municipalities to introduce business regulation reforms at the local level, which opens up opportunities for local agents to predate on enterprises through their manipulation of local business regulation and the discretionary powers they have as local legislators.
- (4) There is a non-obvious relationship between the most extreme form of decentralized agent predation, raidership, and legal and institutional reforms introduced to curb raidership at the central state level. There is evidence to suggest that in Ukraine, the devolving of responsibility for protecting property rights from raidership to local agents has not meaningfully reduced the problem of local raidership, and may even have exacerbated it.

Hopefully, these findings will serve as useful anchor points for future research into the security of property rights at the local level in Ukraine. They give us some idea of where to actually look in local regulatory and political ecosystems for risks of agent predation. My research pinpoints some of the main loci of predation on enterprise at the local level, which could be the basis for future more in-depth case studies. Furthermore, my research reveals some lines of enquiry for future research into the relationship between property rights security and property rights reforms and regulations introduced by national legislature. In particular, my analysis of the gap in regulatory commitment between central state actors and local councils suggests that there is a lack of institutional pressure or mechanisms by which the central state can ensure that reforms are implemented by local authorities.

This introductory section will conclude with a detailed outline of the research gap that I am seeking to address. Then follows a review of the literature and theoretical framework that I will be using to inform my analysis of dependent variable, *decentralized agent predation*. The next section will cover the research methods and methodology used in the thesis. The next four sections will explore the dependent variable and outline the main findings by examining the phenomenon of decentralized agent predation in Ukraine in four different contexts: (1) The State Fiscal Service, (2) Local State Regulatory Agencies, (3) Local Councils and Municipalities and (4) Raidership. In the last section, I summarize my findings and end with a bibliography.

## The Research Gap: Disorganized Predation at the Local Level

In studies of Ukraine's economic and political development, the threat posed to private enterprise by the predatory behaviour of local state actors is often subsumed within the wider topic of corruption. The question is: how exactly does the corruption of state authorities and institutions in Ukraine infringe upon the financial wellbeing and/or property rights of firms? Since a pro-European, reform-orientated government came to power in Kyiv in 2014 with a mandate to fight corruption, there has been an obsessive focus from academia and the international community on this issue. However, analysis tends to focus on the issue of corruption in the business climate at the macro level by consulting, for example, nation-wide corruption perception surveys among the general population or business surveys that treat "corruption" as a single variable in their barometers<sup>2</sup>. There is relatively little detailed examination of the precise forms of misgovernance and corruption which afflict Ukraine in specific areas, such as relations between private enterprise and local or regional authorities. Furthermore, analysis of the impact of anti-corruption reforms in general tends to be restricted to their implementation at the national and central government level – for example, the establishment of national anti-corruption agencies and a national anti-corruption court – without as much attention paid to how these efforts are being reflected or emulated at the local government level.

This thesis will not dare to confront the overwhelming question of corruption in the business climate of Ukraine as a whole. However, it will attempt to fill a research gap that has been left by the preponderant emphasis in the scholarly literature on "grand corruption" at the parliamentary and national level in Ukraine's institutions, by analysing a specific aspect of misgovernance in Ukraine; that is, *the threats posed to Ukrainian private enterprises by the predatory behaviour of local and regional authorities and other state agents*. The "authorities" in question here include local officials, bureaucrats from administrative agencies and politicians at the local government level. Notice that we are concerned not only with agents officially representing the local or regional administration, but also bureaucrats from the local branches of state agencies (such as the tax administration service, regulatory agencies etc.) who are "decentralized" agents to the extent that they operate and apply their discretionary powers within a defined area. As we shall see, the "threats" and "predatory behaviour" being examined will cover a spectrum of corrupt activity ranging from rent seeking to outright raidership (i.e. full expropriation of private companies). Although it is a cliché to state that even in post-Maidan Ukraine property rights are poorly protected and private companies are at a high risk of

expropriation or rent seeking from corrupt officials, there has been insufficient critical examination of where exactly these risks come from; what parts of the state apparatus can be used to target firms for rent-extraction or expropriation, and what kind of discretionary powers are employed to this end?

## Literature Review

### Property Rights and Institutional Constraints on Predation

We are interested primarily in the actions of state authorities, bureaucrats and officials at the local government level and in decentralized state agencies who abuse their discretionary powers to extract rents and even threaten the property rights of private firms. To answer my research question and examine the relationship between institutional constraints and agent predation, I will be focussing on two main branches of the theoretical literature: the literature on property rights and the literature on principal-agent relations. We have elected to focus on *property rights* conceptually because threats to property rights transcend the vague phenomenon of “petty corruption” and constitute those aspects of misgovernance which can seriously and ruinously affect the health of private enterprise. This research focus leads us inevitably into the academic literature on property rights (PR); how they are established and how they are defended, especially in developing post-soviet economies with imperfect democratic institutions, such as Ukraine. In particular, we will need to examine the theoretical relationship between property rights and the principal-agent problems that emerge when political systems attempt to restrain or control threats to these rights; how do different political regime types seek to ensure that property rights are defended even at the agent level, or at least that they are only threatened in the state principal’s interest?

For our purposes, we shall follow Barzel (1997) in broadly defining “property rights” as a triplet of rights: (1) the right to receive income from assets, (2) to use and manage those assets, and (3) to transfer them<sup>3</sup>. As we shall see, there may be some analytical value to be gained from distinguishing between (1) as “income rights” as opposed to (2) and (3) which could be classified as “ownership” rights (more on that later). Some scholars have theorized ways in which property rights might be generated by an autocratic political system. In an influential article, Olson (1993)<sup>4</sup> famously conceptualized the autocratic state principal wishing to maintain control over his subjects whilst maximizing his tax revenue as a “stationary bandit”. In primitive, pre-autocratic societies without any semblance of law or order and the absence of a monopoly over violence, Olson reasons, the security of property rights is constantly in jeopardy; whatever is produced is at risk of being plundered or destroyed by “roving bandits”, whose only incentive is to maximize the proceeds of their plunder whilst roving from village

---

<sup>3</sup> Yoram Barzel, “Economic Analysis of Property Rights”, Cambridge: Cambridge University Press, 1997

<sup>4</sup> Mancur Olson, “Dictatorship, Democracy and Development”, *The American Political Science Review*, Vol. 87, No. 3 (Sep., 1993), pp. 567-576

to village. This precarious state of affairs in turn destroys any incentive for producers to invest for the future or to expand, and renders economic development highly improbable. An important transition comes when one of these “roving bandits” decides to remain and establish dominion over a particular territory and extract as much wealth as possible from the producers who inhabit it. To state Olson’s argument in the briefest terms, in such a scenario the incentive structure for the bandit changes; he has now a stake in providing a system of government and ensuring a degree of law and order that would allow for economic development, since he can extract far more from producers on his territory in the form of tribute formalized as tax revenues than he ever could from itinerant predation on these producers. For Olson, then, the notion of an autocrat (or any other state principal, for that matter) being described as “predatory state” is misguided; rather, by establishing a regular and predictable system of rent extraction, or a “*monopoly of theft in his domain*”<sup>5</sup>, in which producers can be defended from predation by other bandits, the stationary bandit resembles “*the rancher who makes sure that his cattle are protected and given water*”<sup>6</sup>.

Olson’s conceptualization of the rational stationary bandit is important, not necessarily because it is an accurate account of autocratic incentives or how rule-governed states come to be established but because its perspective informs and explains much of the literature on property rights, inasmuch as it focuses on the capacities and incentives of the *state principal* rather than *state agents* in explaining PR threats. A great deal of literature in political science and development economics, for example, is devoted to explaining how property rights are secured when institutions are developed which can place constraints on the discretionary powers of the central state executive to predate. Authors such as Acemoglu and Robinson (2012)<sup>7</sup> and North and Weingast (1989)<sup>8</sup> argue that citizens and private enterprise are protected from predation when the ruler “commits” to institutional constraints which would make the costs of theft from businesses or private citizens prohibitive; in the words of Acemoglu and Robinson, property rights are secured by states with “*inclusive political institutions where power is constrained and broadly distributed*” and where the political power of the principal and the elite are curtailed<sup>9</sup>. These constraints include, but are not limited to, institutions such as adversarial political parties, an independent judiciary, and business associations. Some of these constraints can be more effective than others, depending on the context: business associations are not much use if they are

---

<sup>5</sup> Olson (1993), *op. cit.* pg. 568

<sup>6</sup> Olson (1993), pg. 569

<sup>7</sup> Daron Acemoglu and James A. Robinson, “Why Nations Fail: The Origins of Power, Prosperity and Poverty”, New York: Crown Publishing Group, 2012

<sup>8</sup> “Constitutions and Commitment: The Evolution of Institutions Governing Public Choice in Seventeenth-Century England”, *The Journal of Economic History* 49, no. 4 (1989) pg. 803-32

<sup>9</sup> Daron Acemoglu and James A. Robinson, “Why Nations Fail: The Origins of Power, Prosperity and Poverty”, *op. cit.* pg. 89

financially beholden to the state principal, for example. What many of these theoretical models have in common is that they focus almost exclusively on the constraints that are imposed on the state principal, and treat the potential predatory behaviour of the principal's underlings as a relatively minor concern. In other words, most of the literature underestimates the impact of the central government's local subordinates, lower-level bureaucrats and other agents of the state on PR security; for Levi (1981), the sovereign might threaten property rights, whereas his lower-ranking subordinates can merely threaten "*shirking and venality*"<sup>10</sup>. To sum up, one of the key contentions of the existing political science literature is that *the most important factor determining the security of property rights is the set of institutional constraints placed on the behaviour of the state principal*.

### Markus' Agent Predation: Decentralized Threats to Property Rights

In his 2015 study *Property, Predation and Protection: Piranha Capitalism in Russia and Ukraine*, Stanislav Markus turned his attention precisely to this theoretical blind spot in the literature on property rights; whilst legions of scholars had dealt earnestly with the question of how state principals violate and can be prevented from violating property rights, strikingly little attention has been paid to the phenomenon of property rights being threatened by lower-level, decentralized *agents* of the state apparatus. Markus' crucial theoretical contribution to the debate is to emphasise that "*in modern developing states, government employees attack ownership rights in a way that transcends existing conceptualizations of corruption*"<sup>11</sup>: in particular, state agents at the local level are capable of much more than simply siphoning away income from the businesses under their purview in the form of bribes and rents – they can impact the profitability and security of these businesses' property rights to such an extent that their very existence hangs in the balance.

Scholars writing about corruption have extensively analysed the numerous "principal – agent" problems that arise in any bureaucratic apparatus and that can lead to bribe-taking. Indeed, in one of the first comprehensive scholarly studies of corruption, Susan Rose Ackermann (1978) examined a typical principal-agent relationship between the state principal and a regulatory inspector, observing that the corruption risk is presented when '*some third person, who can benefit by the agent's actions, seeks to influence the agent's decision by offering him a monetary payment which is not passed on to the*

---

<sup>10</sup> Margaret Levi, "The Predatory Theory of Rule", *Politics and Society* 10, no. 4 (1981)

<sup>11</sup> Stanislav Markus, "Property, Predation and Protection: Piranha Capitalism in Russia and Ukraine", Cambridge University Press, 2015

*principal*<sup>12</sup>. Ajit Mishra (2016)<sup>13</sup> draws attention to what we might call the asymmetry that is frequently to be found in the monitoring and accountability dynamics govern the principal – agent – firm relationship; whilst the state agent (for example, a tax inspector) is empowered to examine the minutiae of a business’ activities and penalize the business for its misdemeanours or breaches of the law, there is rarely any comparable level of monitoring or chain of accountability between the agent and the principal itself. These insights are valuable for theorizing the nature of corruption. However, whilst Markus acknowledges that such theoretical attention has been given to the problem of petty, bureaucratic corruption, he contends that in developing states such as Russia and Ukraine these principal-agent problems can be of such a magnitude as to constitute an actual threat to property rights, and that to extend the blanket term of “corruption” of such cases is to underestimate and misdiagnose the problem. Markus develops a “threat type” matrix (shown below) to elucidate the conceptual distinction he makes:

Type of Threats (across): Type of Rights (down):	Organized [ <i>i.e. centralized</i> ]	Disorganized [ <i>i.e. decentralized</i> ]
Income Rights	“SKIMMING”	“SIPHONING”
Ownership Rights	“PRINCIPAL EXPROPRIATION”	“AGENT PREDATION”

Table taken from Markus (2015), pg. 28 (*italics added by the author*)

As we can see, threats to private firms from state agents are classified in two ways: whether they are “organized” or “disorganized”, and whether they affect “income rights” or “ownership rights”. By “organized” we mean here whether the threat is orchestrated or licensed by the state principal (the president/monarch etc.). “Income threats” are small-scale depletions of a firm’s income stream, perhaps in the form of bribes or kickbacks, at the hands of authority – “Ownership threats”, however, refer to those extractive actions which jeopardise the very existence of a firm and/or the security of the owner’s property rights. For the most part, the political science literature on property rights and

<sup>12</sup> Susan Rose-Ackerman, “Corruption: A Study in Political Economy”, New York: Academic Press, 1978, pg. 6

<sup>13</sup> Ajit Mishra, “Corruption, hierarchies and bureaucratic structure” in “The International Handbook on the Economics of Corruption”, (Ed. Susan Rose-Ackerman), Edward Elgar Publishing, 2016, pg. 190

economic development focuses on *organized* threats to free enterprise – that is, threats from the state principal. When the state principal taps the income streams of businesses (in the form, for example, of regular tithes, taxes, levies or “protection fees”), this corresponds to “Skimming” in the matrix. “Principal Expropriation”, on the other hand, refers to cases where the state principal outright targets the assets of business owners and seizes it as their own.

The main focus of this research lies in those two types of threat which the matrix classes as “disorganized”: *disorganized threats to income rights* and *disorganized threats to ownership rights*. Whereas much of the “petty corruption” analysed in the literature refers to what the matrix designates as “Siphoning” (i.e. regular tapping of the business’ income stream by state agents which does not ultimately pose an existential threat to the firm), extractive actions by disorganized agents which are so impactful in their magnitude and/or unpredictability as to threaten the firm’s future are conceptualized as “Agent Predation”. For our purposes, we note that disorganized threats could equally be described as *decentralized*, insomuch as they are not orchestrated or endorsed by a higher authority or through a “power vertical” connecting the state agent to the state principal<sup>14</sup>. The kind of threats to property rights that this thesis examines lie on the right side of the table, and can be categorized as disorganized or decentralized predation – the theoretical distinction between “siphoning” and “agent predation”, whilst plausible, is to my mind too subtle to rigorously delineate in the data with the limited resources of this study. Whether or not predation from a local state actor poses a serious risk to the life of the business or is merely a kind of regular inconvenient tax or cash cost can only be decided on a case by case basis. When applying this framework to the data from the Business Ombudsman’s Office, I am implicitly assuming that if the local threat was serious enough to justify the time and expense required to seek the support of the Business Ombudsman, then it should probably be categorized as an “ownership threat”<sup>15</sup>. I will thus conceptualize *decentralized agent predation*, the main dependent variable, as: *threats to firms’ property rights from local agents who are not a significant actor in a centralized state institution*. An example might be the head official of a local regulatory agency such as the Local Administration’s Department of Ecology and Natural Resources in the City of Kyiv, responsible for ensuring that companies comply with environmental legislation (this is a real agency that we’ll encounter in some examples later). The remit of this agency is restricted to a particular geographical area (the city of Kyiv) and its jurisdiction does not spread any further: whilst it may ultimately be answerable to central state institutions, it is not itself a significant actor in a centralized state institution with powers extending beyond its local remit, and is thus classed as a *decentralized agent*.

---

<sup>14</sup> Accordingly, we shall henceforth use the terms “disorganized threats” and “decentralized threats” to ownership/income rights interchangeably.

<sup>15</sup> This may well be a major limitation to the theoretical distinction between “siphoning” and “agent predation”

A second important contribution of Markus (2015)' work is to question, with empirical evidence, the theoretical orthodoxy in the "state commitment" literature that *institutional constraints on the state principal lead to greater property rights security*. In our literature review, we have already seen that the prevailing theory amongst political scientists is that when the state principal makes credible commitments to constraints on their executive power, the impact of the predatory state on private enterprise is curtailed. In the post-soviet region, these constraints often take the form of a new constitutional arrangement which forces the state principal into power-sharing with other actors, such as a parliament. Markus offers a counterexample to this position in his analysis of the state of property rights security in Ukraine following the "Orange Revolution" in 2004. After large-scale protests (which were supported and attended by thousands of entrepreneurs from small, medium and large sized Ukrainian businesses) had thwarted the falsification of the presidential election, a new president, Viktor Yushchenko, came to power with an agenda of achieving economic development through protection of property rights, democratic reforms, and institutional constraints on executive power. The president duly made several credible legislative and institutional commitments (on the *central* level) to property rights security, and a more balanced constitutional system was introduced, whereby the president's powers were checked by the Ukrainian parliament, the Verkhovna Rada<sup>16</sup>. However, what actually happened following the Orange Revolution and the imposition of institutional constraints on the principal was almost precisely the opposite of what the theoretical literature predicts: whilst Ukraine saw its political freedoms increase dramatically during the years of the Yushchenko presidency and developed a genuinely pluralistic and competitive political system for the first time in its history, the security of entrepreneurs' property rights deteriorated and the overall level of corruption in the country worsened, according to business survey data and the metrics of international observers such as the World Bank's "Governance" indicators<sup>17</sup>.

Accounting for this development, Markus presents the testimony of Ukrainian entrepreneurs and country experts to the effect that the decentralization of power unleashed by the institutional changes enacted by the state principal following the Orange Revolution, and the collapse of the previous presidents' "power vertical", which had at least kept some check on the behaviour of egregiously predatory agents, led to a wave of predation on business by opportunistic bureaucrats on the local level from the year 2004 onwards. It turns out, then, that in the case of Ukraine's Orange Revolution, constraints imposed on the state principal might have actually exacerbated the problems of "agent/decentralized predation" on the ground across the country. These findings will be relevant to our own analysis of the state of agent predation in post-2014 Ukraine, as the Euromaidan protests of

---

<sup>16</sup> Markus (2015), pg. 152

<sup>17</sup> *Ibid*, pg. 154

that year triggered a comparable shattering of the previous presidential power vertical and state commitments to property rights security, in the form of a vision a more “European” Ukraine. Markus’ account of the centrifugal predatory forces unleashed by the Yushchenko presidency will be particularly pertinent in the light of successive post-Maidan governments’ commitments to an ongoing decentralization reform which, it is argued, will devolve as much decision-making power as possible from the central government to local authorities<sup>18</sup>.

Other theoretical and empirical research on threats to property rights in post-soviet states have yielded valuable insights into the importance of the local political and institutional environment for the security of property rights, and how institutional constraints inscribed into law and institutions at the central level are not necessarily translated into effective property rights regimes on the ground. For example, Allina-Pisaro’s (2007) study of the privatization of land in the Black Earth region of Russia and Ukraine after 1991 concludes that the redistribution of land through legal norms and constraints introduced by the central state did little to change the cultural practices and informal institutions that determined development on the local level, and in many cases led to even worse impoverishment and property rights insecurity than before<sup>19</sup>.

To conclude, our main dependent variable, the phenomenon of *decentralized agent predation* on private enterprise, is still comparatively neglected by much of the recent analytical work on the problems of corruption and misgovernance in Ukraine, hence the need to address this research gap. I have conceptualized this dependent variable as “*threats to firms’ property rights from local agents who are not a significant actor in a centralized state institution*”.

## The Research Gap in Contemporary Studies of Ukraine

Although the tumultuous events of 2013/2014 and the “European choice” made by the Euromaidan protestors and the governments that have been elected since then have triggered an upsurge in academic and journalistic writing about tackling Ukraine’s corruption problem, relatively little scholarly attention has been paid to the status of property rights protection for private enterprise in Ukraine, and the success of government and civil society reformers’ efforts to address the threats posed by rent-seeking and other extractive assaults on Ukrainian business. This is not surprising – after all, it is a lot

---

<sup>18</sup> Andreas Umland: The International Effects of Decentralization, Vox Ukraine, 30.1.2019 (<https://voxukraine.org/en/international-implications-of-ukraine-s-decentralization/>)

<sup>19</sup> Allina-Pisano, Jessica – “The Post-Soviet Potemkin Village: Politics and Property Rights in the Black Earth”, Cambridge University Press, 2007

easier, especially for external observers, to describe the progress of centralized, high profile institutions based in Kyiv, such as NABU, in convicting nationally known fraudsters than it is to summarize how much Ukrainian businesses are being forced to line the pockets of petty bureaucrats in Zaporizhia, Bakhmut, or a remote village in the Carpathian mountains.

The threat of local state agents to Ukrainian businesses is often subsumed under the rubric of “corruption”, and swallowed up in the oceans of literature being generated on this topic. Of course, the distinction between higher level, organized corruption at the political centre and disorganized, decentralized corruption and/or predation is important and often alluded to in the literature. However, in much of the recent academic analysis and commentary on the situation in Ukraine, the supposedly distinguishing characteristics of each of these forms of corruption are too sharply drawn, belittling the threat posed by decentralized corruption (including to private enterprise), and thus decentralized agent predation by grouping it with small scale “petty corruption”, and thus mischaracterizing it as mostly referring to the bribes and other informal payments that citizens are regularly required to pay to public officials in order to “get things done” with minimum hassle and to access services. For example, one of the most authoritative and widely cited recent assessments of Ukraine’s battle against corruption since 2014, the Institute for Economic Research and Policy Consulting’s excellent report *Ukraine’s Fight Against Corruption: The Economic Front*<sup>20</sup>, sets out the three traditional “functional types” of corruption around which their research is structured:

- a) Political corruption – which is the manipulation by politicians with political decisions, rules, procedures and institutional activities in the area of resource allocation and financing, and also abuse by politicians of their powers to retain and increase their authority, assets and private gain
- b) Large-scale (grand) corruption covers actions committed by the top-level officials to obtain the benefit at the expense of society by means of exercising the distortive influence on the government policy and the government functioning mechanisms at the central (national) level
- c) Small-scale, or petty, corruption is a daily abuse of powers by the mid and low-level officials in the process of their interaction with citizens seeking to solve personal problems

*“Ukraine’s Fight Against Corruption: The Economic Front”, IERP, pg. 11*

Notice that what chiefly separates types a) and b) from c) is that the former are concerned with personal enrichment at the public’s expense by high-ranking officials or politicians with their hands on the levers of power, and mostly deal with actors at the central level – although a) could of course also refer to regional and local politicians, at least those with control over “resource allocation and financing” and

---

<sup>20</sup> Institute for Economic Research and Policy Consulting (IERP), “Ukraine’s Fight Against Corruption: The Economic Front” November 2018  
([http://www.ier.com.ua/files/publications/Policy\\_papers/IER/2018/Anticorruption\\_Report\\_EN.pdf](http://www.ier.com.ua/files/publications/Policy_papers/IER/2018/Anticorruption_Report_EN.pdf))

with authority and assets worth protecting. Everything else is categorized as c), small scale or petty corruption, the kind associated with “citizens seeking to solve personal problems”, rather than, say, private enterprise. However, this tripartite typology does not include an important category of corrupt activity which, as we have seen, has long proven itself to be a menace to Ukraine’s business community and the country as a whole. What is missing in this typology of corruption is precisely the kind of “disorganized predation” that the literature on property rights in post-soviet states identifies. Agent predation is not necessarily “political corruption” (the official who turns up to fine your business for not complying with some fictitious tax regulation is not a “politician” with control over “resource allocation and funding”), certainly not “large, grand scale corruption”, and can hardly be classified as “petty corruption”, when it carries the risk of threatening property rights. Accordingly, this phenomenon of decentralized predation will be our point of focus in our examination of the relationship between decentralized state agents and Ukrainian firms.

## Research Methods and Methodology

### Research Methods

I have conceptualized the main dependent variable, *decentralized agent predation*, as “*threats to firms’ property rights from local agents who are not a significant actor in a centralized state institution*”. This variable which defies easy description; is not easily captured in any of the qualitative or quantitative surveys that are commonly carried out by analysts of Ukraine, and is extremely difficult from a data collection standpoint to disentangle from the amorphous juggernaut of “corruption”. Nevertheless, there are a range of qualitative and quantitative sources that can be drawn upon to trace the nature and impact of agent predation on Ukrainian firms, and which will form the empirical basis of this study.

In terms of quantitative data, business surveys such as the World Bank’s Environment and Enterprise Performance Survey (BEEPS) and others that are Ukraine-specific (many of which are only available in Ukrainian), such as those carried out by USAID’s Leadership in Economic Governance Programme (LEV), offer an excellent starting point for analysing country-wide trends in the country’s business environment. Because these surveys track variables that specifically gauge problems of misgovernance and corruption, when interpreted carefully and with the appropriate caveats they can inform our understanding of the dynamics of agent predation. We are also quite fortunate in having access to a relatively new and potentially very rich source of data on disputes between Ukrainian (and foreign) businesses and state agencies, both at a national and local level: the Business Ombudsman Council of

Ukraine (BOC)'s database of complaints submitted by private companies to the Business Ombudsman for alleged infringements of the law and/or corrupt and extractive activities against business. The BOC was set up by the European Bank of Reconstruction and Development (EBRD) in 2014 in order to support “*combatting corruption in Ukraine*”<sup>21</sup> with financial support from a number of international donor countries, and since then has operated as “*the first point of contact for companies seeking redress against unfair treatment*”<sup>22</sup> in Ukraine. The BOC's team of analysts and investigators have heard over 6,000 complaints from companies large and small from across the entire country, spanning businesses of every kind of industry and involving dozens of different state agencies, and have settled cases with a total combined financial impact of around 13 Billion Hryvnia. The BOC's explicit mandate for combatting corruption and their status as the first point of contact for a company that believes it is the victim of misconduct, rather than simple administrative difficulties, makes its database a valuable source of information for analysing which state agencies and bodies in Ukraine are being accused of wrongdoing by firms, and which might therefore be engaged in agent predation.

I am relying upon these data sources in order to operationalize the dependent variable *decentralized agent predation*, because I assume that these data reflect instances of threats to firms' property rights emanating from a local state agent. In most cases, the data reported are pre-categorized to indicate whether or not the state agent was a local actor or a central state official. For example, the Business Ombudsman data clearly classifies complaints according to whether the complainee was from a “local regulatory agency”, for example. The BEEPS survey data also classifies perceived threats according to whether the source was a “local or regional official”. I am implicitly assuming that these designations are accurate and that in using this data I am operationalizing the *decentralized* element of the dependent variable correctly, although reporting mistakes are always possible.

This desk-based research and quantitative data will be supplemented by qualitative data from 16 semi-structured interviews with a number of individuals who have first-hand experience or considerable expertise in matters concerning relations between government and business in Ukraine. The purpose of these interviews was to establish how prevalent predatory and/or rent-seeking activity by decentralized state agents against private companies is in post-Euromaidan Ukraine, and to identify what instruments, agencies or techniques are used by these authorities against their victims. Hence, the main criterion for selection were that the respondent has first-hand and extensive stakeholder experience of local government-business relations in Ukraine. The results of the interviews could thus be used to build up an empirically based overview of how firms' property rights are threatened by local

---

<sup>21</sup> Business Ombudsman Council of Ukraine Website, <https://boi.org.ua/en/>

<sup>22</sup> Ibid.

agents in post-Maidan Ukraine. I typically sourced the respondent through one of two ways: (1) After reading material written by the respondent which, corroborated by other expert opinion such as my colleagues at the Eurasia division of Stiftung Wissenschaft und Politik (SWP), convinced me that they would provide valuable insight into the dependent variable, or (2) Recommendations from colleagues during my internships at SWP, UNDP or the scholar Duncan Leitch. I was introduced to Dr Leitch by a contact at the UK embassy in Ukraine in 2018, and his extensive experience of working with local governments in Ukraine and Russia since 1993 made him a highly reliable and credible source of contacts for my research question.

The interviews were conducted either in English or Russian, and took place in various locations as well as over Skype. The respondents were drawn from a variety of backgrounds, from Ukrainian businesses to international experts engaged in development projects in Ukraine; there are representatives of Ukrainian business associations, institutions such as the Business Ombudsman Council of Ukraine, Ukrainian NGOs specializing in economic development and business regulation, international advisors for projects aimed at stimulating and improving the business environment in Ukraine, and even officials from the Regional Administration of Boryspil Rayon (county), Kyiv Oblast. The selection of respondents tried to capture a wide a range as possible of different expert voices on the dependent variable: hence the inclusion of state insiders (the Boryspil officials), as well as anti-corruption activists, Western and local NGOs. The idea behind this is that each respondent will necessarily bring to bear only a partial view to the topic of the thesis based on their professional background and allegiances, and will bring their own biases to the problems discussed as well – hence, in order to obtain a well rounded view of the problem, the optimal respondent selection would include actors from different corners of Ukraine’s civic and institutional ecosystem.

The questions fielded to the respondents and the conversations that unfolded were designed to be as open ended as possible, so as to avoid steering the respondents into any particular answer or to introduce framing biases into the questions that might weight their answers in a particular way. For example, rather than addressing the topic of disorganized state predation directly, the first question relevant to the thesis that I typically fielded was: *“What do you think are the main problems facing businesses in your local area?”*. If the respondent voluntarily mentioned the risks posed to enterprises by local state actors, I would ask them to specify how the actions of these state agents impinged on the property rights of firms and what instruments were used. These descriptions would help to lend context to the data from the Business Ombudsman’s Office and other sources.

The respondents were all contacted directly, with the exception of the 4 local officials from Boryspil Rayon, who were contacted through a family friend. The table below shows the composition of respondents from the semi-structured interviews:

Name of respondent and how they were sourced	Language in which interview was conducted	Location and Date of Interview
Representative of Transparency International Ukraine Source: recommendation from colleagues at UNDP	English	Respondent's office in Kyiv, October 2018
Anna Popova, Ukrainian Network of Integrity and Compliance (UNIC) Source: recommendation from colleagues at UNDP	English	Respondent's office in Kyiv, November 2018
Sebastian Veigler, Chief Consultant, GIZ Ukraine Source: recommendation from colleagues at SWP	English	Over Skype, February 2019
Irina Stanislavska, Business Ombudsman Council of Ukraine Source: recommendation from Duncan Leitch	Russian	Over Skype, March 2019
Roman Dmitriv, Head of Hora Silska Rada (Hora Town Council), Boryspil Rayon Source: Author's research	Russian	Respondent's Office in Boryspil, April 2019

Oleksandr Lazarenko, Head of Gnidinska Silska Rada (Gnidina Town Council), Boryspil Rayon Source: author's research	Russian	Respondent's Office in Boryspil, March 2019
Head of Kuchakiv Silska Rada (Kuchakiv Town Council), Boryspil Rayon Source: author's research	Russian	Respondent's Office in Boryspil, April 2019
Deputies of the Head of Boryspil Regional Administration Source: author's research	Russian	Respondent's Office in Boryspil, April 2019
Vladimir Dubrovskiy, Chief Economist, CASE Ukraine Source: author's research	English	Over Skype, May 2019
Vira Nedzvedska, Legal Expert at Eastern Europe Foundation Recommendation from Vladimir Dubrovsky	English	Over Skype, May 2019
Oleksei Dorogan, Deputy Head of Better Regulation Delivery Office (BRDO) Source: author's research	English	Café in London, May 2019
Irina Lekh, Entrepreneur and Head of "Porada" Business Association	Russian	Over Skype, June 2019

Source: recommendation from Duncan Leitch		
Vladislav Baichas, Head of Boryspil Rayon Council Source: author's research	Russian/Ukrainian	Respondent's office in Boryspil, June 2019
Representatives of American Chamber of Commerce, Ukraine Source: author's research	English	Respondents' offices in Kyiv, June 2019
Yevhen Popov, Anticorruption activist, "Open Odesa" Source: recommendation from colleagues at UNDP	English	Over Skype, June 2019
Kadie Ward, Consultant at PLEDDG (Partnership for Local Economic Development and Democratic Governance) Source: author's research	English	Over Skype, July 2019

## Methodology

The methodological problems raised by the methods adopted for this research are serious, far reaching, and necessitate a highly conservative approach to interpreting our findings. With a topic such as this, the researcher cannot hope for an exhaustive supply of quantitative or qualitative evidence to draw upon for sure-footed conclusions regarding the threat posed to private businesses by predatory local authorities in Ukraine; even the most authoritative data collected at the national level on subjects such as corruption in the private sphere do not reach very far into specific variables beyond the stated figures

of corruption perception, and to my knowledge there has not been any serious systematic attempt to address the question of small-scale predation on private enterprise in Ukraine since 2014. Predation by local authorities and state agents is not among the variables considered by any of the major corruption surveys conducted in Ukraine over the last decade or so. However, this does not mean that there is insufficient material in the secondary literature, combined with qualitative evidence drawn from interviews with stakeholders who have first-hand experience of this issue (including business owners, civil society activists, and representatives of business associations) and quantitative data from the Business Ombudsman Council of Ukraine's database of complaints addressed submitted by Ukrainian businesses, to build up an informative picture of the extent and nature of the threat that businesses in Ukraine face on the local level from the ranks of administrators and bureaucrats of local government.

From a researcher's perspective, methodology is not so much the sources of information and evidence that one draws upon in order to reach conclusions, but the epistemological stance taken in regard to this collected evidence and the research question at hand; how can we be confident that this data really reflects the current state of affairs on the ground in Ukraine, as far as the relationship between local state agents and business is concerned? On the quantitative side, the researcher makes no claim to statistically rigorous conclusions drawn from the BOC's database of complaints. Serious questions of validity arise when using this data; given that we are looking at only a selection of companies who are, firstly, aware of the institution of Business Ombudsman and, secondly, prepared to entrust it with their grievances, we must question whether these complaints are truly representative of private enterprise in Ukraine as a whole. This is especially true given that the variable we are investigating, *small scale predation by decentralized state agents*, is pertinent to many smaller local companies that, as a class, are probably less likely to be aware of the possibility of seeking redress from the BOC, and therefore our data pool may be disproportionately skewed towards larger, internationally well-connected companies – although around 75% of the companies that appeal to the BOC are small or medium sized companies, and roughly 15% are foreign owned<sup>23</sup>. The same concern applies, arguably to a much greater extent, to the qualitative data derived from semi-structured interviews; it would be unwarranted to treat the concerns and opinions raised by these respondents as representative of Ukrainian business as a whole. However, the aim is not to build statistical conclusions based solely on the evidence from interviews – they serve rather as a source of insight into whatever patterns and variables might emerge as worthy of more attention in this field, and which might shed some light on the more representative data found elsewhere.

---

<sup>23</sup> BOC IV Quarter Report, 2019 ([https://boi.org.ua/media/uploads/q42018/q4\\_2018\\_en.pdf](https://boi.org.ua/media/uploads/q42018/q4_2018_en.pdf)), pg. 7

There are also validity concerns regarding the data on complaints against local authorities, and the extent to which cases involving wrongdoing by local authorities necessarily reflect deliberate and malign predatory activity by these agents. Nevertheless, the impressive geographic coverage of the BOC's data and the sheer number of cases submitted, allows us to say with some confidence that they at least allow us to examine *how large certain problems related to corruption in the private sector (such as local authorities' preying on business) loom in the minds of businesses in Ukraine that are engaged and concerned enough by these problems to seek the support of the Business Ombudsman Council.* Whilst this will not yield an authoritative, comprehensive assessment of the role played by these dynamics across the whole of Ukraine, it is hoped that it could serve as an illuminating starting point for future research, directing us towards issues that might continue to be salient for post-Maidan Ukraine.

## Section 1. Decentralized Agent Predation Threats in Tax Administration

### The State Fiscal Service as Predator: From Kuchma to Yanukovych

According to a host of scholars and Ukraine observers, one of the main vehicles through which opportunistic lower-level state officials have historically been able to exploit their discretionary powers to predate on businesses in Ukraine has been the tax administration system<sup>24</sup>. In his review of Ukraine's economic development since independence, Åslund (2015)<sup>25</sup>, identified this phenomenon as one of the key risks to the business environment and property rights regime in Ukraine. Åslund emphasizes the need to simplify the highly fraught tax administration system, describing an environment in which "competing tax agencies" pursued their own rent-extraction strategies, siphoning as much they could get away with from businesses - which meant that the same companies would often be targeted and forced to pay several times by different agencies<sup>26</sup>. This description of the agent predation problem afflicting Ukraine's tax system is echoed by Dubrovskiy (2015)<sup>27</sup> in his in-depth study of the development of the Ukrainian tax system since independence, and in Lough and Dubrovskiy's (2019) paper assessing the impact of anti-corruption reforms since 2014<sup>28</sup>.

Incidentally, this phenomenon – whereby overlapping tax or other regulatory agencies prey on the same firms in the absence of a coordinating authority – is termed "overgrazing" by some scholars; the practice is pertinent to our discussion because researchers (such as Fan, Lin and Triesman (2009)) have debated whether decentralized political and regulatory systems can be correlated with overgrazing, following the argument that "*The more tiers of government and the more local personnel with pockets to fill, the greater the danger that the rents of office will be "overgrazed"...*"<sup>29</sup> – another term used by

---

<sup>24</sup> See, for example: <https://www.kyivpost.com/business/taxes-inspections-remain-biggest-problems-ukrainian-business.html>

<sup>25</sup> A. Åslund, "Ukraine: What Went Wrong and How to Fix It", Peterson Institute for International Economics, 2015, pg. 72

<sup>26</sup> Ibid.

<sup>27</sup> Vladimir Dubrovskiy, "The Political-Economic and Institutional Issues of The Ukrainian Tax System. Part III", *Vox Ukraine*, 07.22.2015 ([https://voxukraine.org/en/the-political-economic-and-institutional-issues-of-the-ukrainian-tax-system\\_eng/](https://voxukraine.org/en/the-political-economic-and-institutional-issues-of-the-ukrainian-tax-system_eng/))

<sup>28</sup> John Lough and Vladimir Dubrovskiy, "Are Ukraine's Anti-Corruption Reforms Working?", Chatham House Research Paper (2018), pg. 14 (<https://reader.chathamhouse.org/are-ukraines-anti-corruption-reforms-working#>), accessed July 2019

<sup>29</sup> Simon Fan, Chen Lin, Daniel Treisman, "Political decentralization and corruption: Evidence from around the world", *Journal of Public Economics*, Volume 93, Issues 1–2, 2009, Pages 14-34,

the authors is “uncoordinated rent seeking” – which in essence corresponds more or less exactly the concept of “disorganized predation”. A Reuters investigation in 2014 reported that, at the time, tax inspectors in Ukraine earned only around \$145 a month, and the head of a regional tax office around \$350 – meaning that, at multiple levels of the organizational hierarchy, officials were strongly incentivized to “top up” their income by exacting informal payments and punitive fines<sup>30</sup>.

Indeed, when surveying some of the post-Maidan evaluations of the shortcomings of Ukrainian tax administration, one cannot help but be reminded of Markus’ description of the disorganized predation by tax officials that was unleashed following the collapse of the Kuchma power vertical in 2004; then, the decentralization of presidential power as exemplified by Yushchenko’s commitment to property rights and constitutional constraints on his own powers resulted in an anarchic scramble on the local level for spoils by predatory officials and local politicians, who took advantage of a political and legal environment characterized by “*The Orange state principal’s lack of control over state agents*”<sup>31</sup> to seize assets and extract rents from firms. Given that Ukraine, at least at first glance, seemed to be suffering from similar problems by 2014, even under the highly centralized presidential system created by Yanukovich, does this mean that the widespread “disorganized agent predation” so characteristic of the post-Orange Revolution era continued to seriously afflict the business climate under Yanukovich? And if so, does this suggest that Ukraine’s disorganized agent predation thrives in highly centralized political frameworks just as well as it does in comparatively decentralized ones?

On closer inspection, however, it would in fact be inaccurate to describe the failings of the tax administration system under Yanukovich as identical to those diagnosed by Markus. The salient feature of the disorganized political and regulatory ecosystem described by Markus’ respondents, in which predatory elements of the tax administration thrived between 2004 and 2010, was that it was often opportunistic local actors that felt empowered to target businesses for rents, independently of other like-minded bureaucrats - hence the complaints from business owners (quoted above) about being fleeced by waves of different inspectors and officials from oblast, rayon and municipal level, who were all patrolling the same turf. In contrast, it was characteristic of the Yanukovich period that the most potent instruments of predation in tax administration were reserved for the principal himself (the president and his ruling clan), who ran a country-wide tax fraud scheme in which firms were compelled to pay into “licensed platforms” in order to receive VAT refunds, the main beneficiaries of which were the Yanukovich family and their associates. Thus, rather than disorganized predation by local agents,

---

<sup>30</sup> Steve Stecklow, Elizabeth Piper, and Oleksandr Akymenko, “Here’s How Scams and Shakedowns Brought Ukraine’s Economy to Its Knees”, *Reuters*, 07.08.2014 (<https://www.businessinsider.com/r-special-report-how-scams-and-shakedown-brought-down-ukraine-to-its-knees-2014-07?r=US&IR=T>)

<sup>31</sup> Markus (2015) *op. cit.* pg. 154

what really plagued Ukraine's tax administration system most of all during the Yanukovich era, according to the most authoritative assessments of the issue, was the tightly organized rent-seeking machine run by the central sovereign itself. In so far as firms' property rights were threatened by their being compelled to contribute to Yanukovich Inc's VAT schemes, and the sums involved, we could classify this activity as "Principal Expropriation" in Markus' typology matrix of state threats to property rights.

This point can be made more clearly when we consider the development of the Ukrainian tax administration system (currently known as the "State Fiscal Service", SFS) in a historical perspective. The SFS has its origins in the State Tax Administration established in 1996 under President Kuchma and headed by Nikolai Azarov. A geologist by profession, Azarov had little time for the nuances and complexities of market economy tax collection systems, and struggled to grasp the concept that firms' income did not by right automatically belong to the state, but must be legally and fairly levied in a consistent manner. Instead, Azarov fashioned the State Tax Administration into what Vladimir Dubrovskiy describes as "*a discretionary punitive tool in the hands of then President Kuchma*"<sup>32</sup>, designed to extort rents and political compliance from any firms that might dare to defy the president's will. For example, secret tape recordings made by Kuchma's bodyguard Mykola Melnychenko in the president's office were alleged to have caught Azarov describing how, in his capacity as head of the STA, he was able to use his position to pressure business elites into supporting Kuchma's re-election in 1999<sup>33</sup>. In other words, Ukraine's tax administration system was originally set up in such a way as to serve as a fiscal cudgel for the principal's own political and economic ends. The fact that, unusually, the institution was made directly responsible to the president<sup>34</sup> is illustrative of its role as an extractive instrument of the executive. A recent Chatham House research paper recognizes this, describing the SFS (then STA) during the Kuchma days as a "*tool of institutionalized corruption*"<sup>35</sup>. This description is completely consistent with Olsen's concept of the "stationary bandit", who reduces haphazard raiding on private enterprise and ensures a minimum degree of stability and predictability in the business environment in order to reserve all extractive activity for himself. This does not necessarily mean, however, that the impact of this extractive activity on firms' property rights was any better or worse than a scenario in which the principal's extractive monopoly was broken or tightly constrained.

---

<sup>32</sup> Vladimir Dubrovskiy, "The Political-Economic and Institutional Issues of The Ukrainian Tax System. Part III", *Vox Ukraine*, 07.22.2015 ([https://voxukraine.org/en/the-political-economic-and-institutional-issues-of-the-ukrainian-tax-system\\_eng/](https://voxukraine.org/en/the-political-economic-and-institutional-issues-of-the-ukrainian-tax-system_eng/))

<sup>33</sup> Serhiy Rudenko, "Mykola Azarov: Yanukovich's Right Hand Man", *RFERL*, 12.03.2010 ([https://www.rferl.org/a/Mykola\\_Azarov\\_Yanukovichs\\_RightHand\\_Man\\_/1982331.html](https://www.rferl.org/a/Mykola_Azarov_Yanukovichs_RightHand_Man_/1982331.html))

<sup>34</sup> Dubrovskiy (2015), *op cit*.

<sup>35</sup> Lough and Dubrovskiy (2018), pg. 15

In 2005, the Kuchma power vertical that enabled this arrangement to exist was broken, and arguably it became impossible for the presidency to exert such complete personal control over the tax administration system. Kuchma failed to secure the election of his appointed successor, Viktor Yanukovich, and the democratic protest movement known as the “Orange Revolution” ultimately brought not only a new president to power, but also a new constitutional arrangement to the country. As part of the political compromise that secured a peaceful transition from the Kuchma regime to the presidency of Viktor Yushchenko, the Verkhovna Rada transferred a range of important powers from the president to the parliament. This would mean that, henceforth, governance of the country would become more of a balancing-act between the president and the newly empowered prime minister, appointed by the parliament. The implications of this arrangement are well elucidated by Henry Hale’s account of the Orange Revolution and its aftermath in his work *Patronal Politics*; instead of a single patronal network (that of Kuchma) dominating the instruments of the executive, Ukraine’s constitutional reform helped “catalyze a balance of formal and informal power between president and prime minister, two competing pyramids that could not defeat each other...its political machine was not eliminated, only fragmented”<sup>36</sup>. The ensuing years of the Yushchenko presidency reflected, for Hale, his model of competing “patronal pyramids”; each of the main protagonists of Ukraine’s political struggle (the president Viktor Yushchenko, his erstwhile ally and first prime minister Yulia Tymoshchenko, and leader of the “Party of Regions” Viktor Yanukovich) had at their disposal a patronal network of business elites and political allies whose resources could be mobilized in order to defend their patron’s interest and prevent a complete autocratic consolidation of power by one of their rivals. While it might be an oversimplification to refer to the main political forces that competed for control over the country’s parliament and executive as uniformly “patronal networks” (some were undoubtedly more patronal than others), there can be no doubt that the constitutional and political balance of powers in play made it impossible for the state principal (the Ukrainian president) to monopolize a state ministry such as the State Fiscal Service and render it totally subordinate as an extractive tool for his own predatory ends, as Kuchma did.

What is the relevance of all this to the institutional corruption of Ukraine’s State Fiscal Service? The point is that it is possible to roughly conceptualize the tax administration service in Ukraine as passing through different degrees of “centralization” over time, in the sense of the extent to which the state principal was able to monopolize the agency’s enormous discretionary powers as an instrument of predation. We can thus begin to see the impact of this centralization of administrative and informal power in the State Fiscal Service on the “agent predation” phenomenon: when the tax administration

---

<sup>36</sup> Henry Hale, “Patronal Politics: Eurasian Regime Dynamics in Comparative Perspective”, Cambridge University Press, 2014, pg. 13

system in Ukraine was relatively decentralized and freed from a “power vertical”, as it was in the years following the Orange Revolution, centrifugal forces of agent predation were unleashed and led to the wide-scale, localized abuse of discretionary powers by local agents of tax administration so vividly documented by Markus’ research. Conversely, when the State Fiscal Service comes under the relatively centralized control of an autocratic state principal who turns it into his own extractive weapon, the Ukrainian business community is more afflicted by the siphoning away of income from the principal than agent predation. The upshot of this is that *a lack of constitutional constraints on the state principal in Ukraine did not necessarily lead to an increase in decentralized agent predation by local agents in the State Fiscal Service* – indeed, the centralization of the State Fiscal Service under Yanukovich may even have made decentralized predation a less pressing problem, as we’ll see. This suggests that the relationship between constitutional constraints and reforms introduced at the central state level and the practice of agent predation at the local level is more complicated than the theoretical literature might indicate.

To illustrate this point, let’s consider what impact a highly centralized tax administration system controlled by the state principal with minimal constitutional constraints had on reported instances of predation on businesses by the tax inspectorate. The Yanukovich administration is a good illustration of how the establishment of a rapacious “power vertical” in the State Fiscal Service can control agent predation whilst itself becoming the chief concern of the business community as far as threats from tax administration are concerned. After the coalition that had brought Ukraine’s “Orange Revolution” collapsed and Victor Yanukovich won the presidency in 2010, Ukraine reverted to a more “single pyramid” system of governance, with the constitutional powers of the president enhanced and a strong power vertical established. During the Yanukovich presidency of 2010 - 2014, large-scale siphoning from private enterprise and public finances through the tax administration system was orchestrated in a highly centralized and hierarchical manner, with the Yanukovich clan the main beneficiaries sitting at the top of an organizational structure that permeated the State Fiscal Service (SFS) with various rent-extraction schemes and licensed larceny from the state budget on an industrial scale. Although the Ukrainian exchequer had always suffered from a number of tax-evasion schemes, Yanukovich succeeded to a large extent in monopolizing the market in egregious tax fraud and fiscal predation, clamping down on evasion schemes that might be describe as decentralized and beyond his control whilst consolidating his own. After taking office, he quickly took control over the tax evasion and rent extraction machines known as “licensed platforms”, which charged firms large commissions in order to fraudulently apply for VAT refunds on transactions and services that never existed. Reportedly, the majority of the 12-13% charges extracted from businesses for these fraudulent schemes went directly

to the Yanukovich family<sup>37</sup>, who controlled them through the tax authorities and the minister for Revenues and Duties, Oleksandr Klymenko. The highly centralized character of this coercive-extractive system is illustrated by the comments made by the Institute for Economic Research and Policy Consulting’s 2018 report, that “we are talking about an intentionally created vertically integrated system through which businesses were practically forced to carry out the relevant operations...”<sup>38</sup>. At the same time, results from the World Bank’s Environment and Enterprise Performance Survey (BEEPS) for Ukraine between 2005 and 2013 indicate that, on average, companies across the country reported that the threat of rent-seeking from tax agencies actually *decreased* during the Yanukovich period, between 2009 and 2014, accelerating a trend that had been ongoing since 2002:



We can thus see that extraction from the state principal through the tax administration system loomed large in the Ukrainian business climate during the Yanukovich period, compared to the threat of agent siphoning/ predation for businesses across the country as a whole. Yet the state principal’s use of the tax system as an extraction machine for its own ends did not, according to the country-wide BEEPS data, aggravate the problem of agent predation on a country-wide level – in fact, the data suggests the opposite. What this suggests is that the severity of agent predation by tax agencies cannot be easily explained by looking at the legal or institutional constraints that bound the state principal. Now let’s take a closer look of how local predation by tax agencies takes place in Ukraine by examining what has happened since the Yanukovich power vertical broke down in 2014.

<sup>37</sup> Lough and Dubrovskiy (2018), pg. 13

<sup>38</sup> IERPC, Ukraine’s Fight Against Corruption: The Economic Front, *op. cit.* pg. 37

<sup>39</sup> Source: BEEP Surveys, World Bank – the left axis measures the average score given by companies to the question “To what degree is tax administration an obstacle to the current operations of this establishment?”, where 0= no obstacle, 1=minor obstacle, 2 = moderate obstacle, 3 = major obstacle, 4 = very severe obstacle

## Decentralized Threats in Tax Administration Post-Maidan: a case of Recentralization?

Since the Maidan Revolution of 2014, Ukraine has reverted to a more balanced constitutional settlement and model of governance compared to the Kuchma and Yanukovich eras, which most closely resembles the period following the Orange Revolution between 2005 and 2010; the president, whose constitutional powers are relatively constrained, is locked into a form of power-sharing arrangement with the prime minister and his cabinet of ministers, with powers to appoint certain ministerial posts divided between them. In the words of one analyst, using Hale's "patronal" terminology, the change represents "a shift that can be described as going from a "single-pyramid system" to a "competing-pyramid" one"<sup>40</sup>.

Along with the constitutional constraints imposed on the state principal, Ukraine's parliament has enacted a series of reforms of the State Fiscal Service (SFS), aimed at curbing the predatory excesses of the Yanukovich tax pit machine. In the aftermath of the collapse of the Yanukovich presidency, the licensed platform schemes and other tax predation mechanisms were still running, but as Lough and Dubrovskiy note, "on a lesser scale, and no longer centralized as before"<sup>41</sup>. The opportunity gap for tax fraud has shrunk since an electronic system for administering VAT payments for companies was established in 2015, and an automatic online system for VAT refunds (which in the Kuchma and Yanukovich years generated huge profits for the state principal and his allies in the form of kickbacks) in 2017<sup>42</sup>.

Thus, the predatory instruments of the state principal as far as tax administration goes have been curbed. Now we turn to the question of decentralized agent predation in the state fiscal service. What has happened to the army of rapacious municipal, low-ranking tax officials from the Orange revolution period?

Well, taking a macro view, despite structural improvements to the State Fiscal Service since 2014, entrepreneurs have continued to take a gloomy view of the tax administration in Ukraine, which frequently stands near or at the top of lists of the institutions most complained about by Ukrainian firms. For example, the American Chamber of Commerce's 2014-2017 corruption perception survey of Ukrainian firms revealed the tax and customs authorities to be the state body regarded as the second

---

<sup>40</sup> Yuriy Matsiyevsky, "Old Political Habits Die Hard in Ukraine" in "Ukraine in the Poroshenko Era: The Politics of Power, Reform and War", *PONARS Eurasia Policy Perspectives*, September 2017, pg. 52

Ukraine in the Poroshenko Era: The Politics of Power, Reform, and War

<sup>41</sup> John Lough and Vladimir Dubrovskiy, "Are Ukraine's Anti-Corruption Reforms Working?", Chatham House Research Paper (2018), pg. 14 (<https://reader.chathamhouse.org/are-ukraines-anti-corruption-reforms-working#>), accessed July 2019

<sup>42</sup> *ibid*

most corrupt by entrepreneurs, behind the courts<sup>43</sup>. Even the more wide-ranging 2016-2017 survey of over 2,000 Ukrainian small and medium sized firms carried out by USAID's Leadership in Economic Governance Programme (LEV) reported that 27% of business owners listed difficulties with the tax administration system ("обтяжливе податкове адміністрування") as a major obstacle to their businesses – the fourth highest inhibiting factor (behind only low demand, political instability and high taxes)<sup>44</sup>. The Business Ombudsman Council of Ukraine (BOCU) has also highlighted the prevalence of tax administration issues in the complaints issued to the body by businesses; in their yearly report for 2018, they note that a staggering 61% of all cases dealt with by the Council related to tax issues, and the State Fiscal Service was the government body subject to the most complaints, accounting for 1,151 of the 1,792 cases taken on that year<sup>45</sup>. Consequently, it has become commonplace for domestic and international media to refer to tax administration as the most severe threat to the health of Ukrainian private enterprise<sup>46</sup>. However, these figures issued by the Business Ombudsman Council do not necessarily reflect an inordinately high level of agent predation in the SFS, or even corruption. It is important to note that the majority of tax issues under investigation by the BOCU concern cases involving the relatively new electronic online systems for VAT invoices and refunds; in 2018, 60% of tax administration cases related to VAT issues. Thus, the majority of complaints regarding tax involve online systems that have only recently been introduced and which are new to Ukrainian entrepreneurs; as was confirmed in a semi-structured interview with a representative of the Business Ombudsman Council, a significant number of these cases are likely to involve administrative and technological issues rather than accusations of corruption by public bodies<sup>47</sup>. According to the raw data that the researcher was given access to, during the period of the BOCU's operations from 2014 to March 2019, approximately 53% of tax cases related to the new online systems for VAT administration. This is not to say that corrupt activity by the SFS in the determination of VAT and VAT refunds does not occur, only that the sheer volume of queries and complaints related to the new system might have exaggerated the perception that the SFS has been targeting Ukrainian businesses.

---

<sup>43</sup> American Chamber of Commerce in Ukraine, "Results of Chamber Corruption Perception Survey" ([http://publications.chamber.ua/2018/Chamber\\_CPS\\_2017.pdf](http://publications.chamber.ua/2018/Chamber_CPS_2017.pdf)); "Tax and Customs authorities" are given a corruption rating of 54%, compared to 71% for the courts. Admittedly, the vagueness of the methodology and metric used for this part of the survey limits its usefulness (what does the 54% correspond to?)

<sup>44</sup> Щорічна оцінка ділового клімату (ABCA, Annual Business Climate Assessment), USAID Leadership in Economic Governance Programme, 2017, *op. cit.* pg. 44

<sup>45</sup> Business Ombudsman Council, "Annual Report 2018", pgs. 14, 19

<sup>46</sup> E.g. Bermet Talant, "Taxes, inspections remain biggest problems of Ukrainian business", *Kyiv Post*, 05.11.2016 (<https://www.kyivpost.com/business/taxes-inspections-remain-biggest-problems-ukrainian-business.html>), accessed

<sup>47</sup> Interview with Representative of Business Ombudsman of Ukraine, conducted by the author over Skype, March 2019

On the other hand, despite the enduringly rotten reputation of Ukraine’s State Fiscal Service, evidence from semi-structured interviews conducted by the author suggest that over the past few years, opportunities for *decentralized agent predation* in the State Fiscal Service have been reduced – and whilst there is no single metric that could convincingly corroborate this, business survey data does not contradict it. Curiously, this improvement is attributed to an organizational centralization of its activity, on the basis of oblasts. In a semi-structured interview with the author, Vladimir Dubrovskiy, chief economist at the think tank CASE Ukraine, who has written extensively about and researched changes in Ukraine’s tax system over the past two decades, stated that tax inspection offices at the local and municipal level (of the kind referred to in Markus (2015), discussed earlier) has been largely done away with in Ukraine, and that tax inspections are now “*concentrated at the oblast [regional] level*”<sup>48</sup>. Essentially, this means that the tax administration system no longer has local branches in Ukraine’s villages and municipalities, meaning that opportunities for individual tax inspectors based in some locality to predate on businesses in their area without fear of reprisal are not nearly so extensive as before. Additionally, the reorganization of tax inspections at the oblast level has meant that tax inspection agents are less able to collude with the local authorities in villages and municipalities in order to target firms for rent seeking or predation. According to Dubrovskiy, eliminating this decentralized collusion between local authorities and tax inspectors was one of the aims of the reform; “*Previously they [local branches of the SFS] were part of the centralized structure of the SFS but they indeed had connections at the local level...one of the reasons that we had to undertake this reform was that we realized we needed to somehow break these connections at the local, which were the most non-transparent part of the system...*”<sup>49</sup>. As a result, the threat of agent predation from state inspections for local businesses on the ground in Ukraine is diminished. In his view, the companies that nowadays at the greatest risk of predation are larger companies whose revenues and operations are consequential at the oblast level and thus might draw the predatory gaze of the SFS’ oblast agents, since the organizational restricting has meant that “*they [SFS agents] are no more connected with local authorities but they are at a higher level...which means they can still harass some businesses but maybe a larger business but on the order of oblast authorities, not the rayon level.*”<sup>50</sup>

Dubrovskiy’s contention that agent predation by the State Fiscal Service is now more of a problem for larger businesses is not contradicted by business survey data; for example, in its discussion of the obstacles facing the business community, the 2016-2017 LEV business survey of Ukrainian firms raised the point that larger firms seem to find tax administration more of a threat than small ones; “*більший*

---

<sup>48</sup> Interview with Vladimir Dubrovskiy, conducted by the author in May 2019

<sup>49</sup> Ibid.

<sup>50</sup> Interview with Vladimir Dubrovskiy

розмір підприємства, тим більш проблематичним для нього є адміністрування податків та бухгалтерський облік..” (“the larger the business, the more problematic tax administration and accounting is for them”)<sup>51</sup>. Of course, this is not quite the same as claiming that agent predation is more prevalent for larger businesses than small, but if the local tax administration scene really were inundated with agent predators as it was in the years following the Orange Revolution then we would expect the business data survey to register this. In another semi-structured interview with the author, Vira Nedzvedska, a legal expert from the East Europe Foundation (an organization that works on economic and political development projects in Ukraine), seconded this assessment of the “recentralization” of Ukraine’s State Fiscal Service, but commented that whilst this has decreased the problem of agent predation, it has “*not abolished it completely, since the chair person [of the SFS] on the oblast level can still be involved with the authorities...*”<sup>52</sup>. That is, agents of the SFS at the oblast level can still collude with oblast authorities and even heads of some municipalities in predation on firms. As Nedzvedska puts it, “*formally they [the SFS] have only service functions, but in fact (I’m not talking about 100%, but partially) they provide bribes from business to oblast level and they help to “solve problems”, they help to create problems...*”<sup>53</sup>.

Indeed, if we wish to appreciate the still considerable potential for agent predation that rests in the State Fiscal Service at the Oblast level, we need look no further than the case of Mychail Gagarkin, who was Deputy Head of the SFS branch in Kharkiv Oblast in 2015, and a classic example of a decentralized agent predator<sup>54</sup>. During his brief time in the position, Gagarkin was accused of “sickly profiting through pressure on business”<sup>55</sup>, obstructing the operations of businesses and forcing them to “deal with him personally”, and pay for the ability to trade free from harassment from his agency. On a smaller scale, the Business Ombudsman of Ukraine’s reports are a useful source of examples showing how oblast level tax inspectors and authorities still routinely abuse their putatively wide discretionary powers and the arcana of Ukrainian legislation to opportunistically extract payments from firms<sup>56</sup>.

Legislative changes introduced by the Verkhovna Rada have in some circumstances made it easier for Ukrainian firms to seek redress against the predatory behaviour of tax agents, but all too often the path to restitution is slow and cumbersome, with the firm accumulating economic losses in the meantime,

---

<sup>51</sup> Щорічна оцінка ділового клімату (ABCA, Annual Business Climate Assessment), USAID Leadership in Economic Governance Programme (2017), pg. 29

<sup>52</sup> Interview conducted by the author with Vira Nedzvedska over Skype, May 2019

<sup>53</sup> *ibid*

<sup>54</sup> (<https://blogs.korrespondent.net/blog/business/3526144/>)

<sup>55</sup> *Ibid*, (“нехило нажився на притесненнях бізнеса”)

<sup>56</sup> E.g. Business Ombudsman of Ukraine “SFS drops additional payment worth UAH 673k against company from Kharkiv Oblast”, 14.06.2019 (<https://boi.org.ua/en/case-studies/303-dfs-skasuvata-donarahunannya-na-sumu-673-tis-grn-pidpriyemstvu-z-harkivshini/>)

and takes place not through conventional channels but thanks to the intervention of a third party, such as the Business Ombudsman of Ukraine. For example, in one case summarized in the Business Ombudsman's 2018 report, a firm from Luhansk Oblast that had had its property confiscated in an inspection by the SFS was able to take advantage of a law newly passed by parliament, the #MaskShowStop law, to appeal against the SFS' delayed handling of their case. As a result, the Business Ombudsman's investigator intervened and wrote to the Prosecutor's Office and Director of the SFS in Luhansk Oblast, demanding that the firm's property be returned. As a result, the firm received their confiscated laptops, hard drives and documents back – almost two years after the tax police had taken them away in an inspection!<sup>57</sup>

## Section 2. Decentralized Agent Predation in State Inspectorates and Regulatory Agencies

In the previous section, a full discussion was devoted to the threats posed to Ukrainian business by the State Fiscal Service (and its antecedent, the State Tax Administration) because this institution had been singled out by authors as uniquely devastating in its impact on the income and property rights of firms. However, there are plenty of other state inspectorates and regulatory agencies operating in the country whose discretionary powers to fine and halt the business operations of firms might put them in an ideal position to extract bribes and/or imperil property rights; these include agencies dealing with ecological standards, work-place safety and labour regulations, planning and architectural norms, and so on. In the hands of unscrupulous operators, these regulatory agencies can be a potent instrument for siphoning off funds from the firms that they are responsible for overseeing.

The rent-seeking approach still commonly employed by officials from these types of agencies, and the risks posed by the discretionary powers granted to them, is regularly touched upon in the literature on PR threats in developing countries. The picture goes something like this; inspectors arrive at the premises of the business, announcing that they are conducting an unscheduled inspection. In due course, an inspection is conducted and violations in the company's practices and working environment are inevitably discovered. This will happen because usually, business regulation in countries such as Ukraine is so convoluted and abstruse that it is impossible or impractical for companies to fully

---

<sup>57</sup> Business Ombudsman Council of Ukraine, "Annual Report 2018", pg. 50-51 ([https://boi.org.ua/media/uploads/annual2018/annual\\_report\\_2018\\_en.pdf](https://boi.org.ua/media/uploads/annual2018/annual_report_2018_en.pdf))

comprehend and implement, and the function of inspection agencies works on the basis of “*selective implementation of impracticable laws*”<sup>58</sup>. As with predation in tax administration, such threats can be orchestrated from the very top of the power-vertical as well as from the bureaucratic undergrowth. During the 1990s, for example, the abuse of regulatory agencies’ powers in predation on business became particularly associated with Pavlo Lazarenko, who served as prime minister under the administration of Leonid Kuchma and extracted huge sums of money in bribes from Ukrainian companies by subjecting them to the country’s highly impracticable and stringent (and previously largely ignored) Soviet-era environmental regulation<sup>59</sup>. In his empirical examination of the threats faced by private entrepreneurs from these kind of state bodies, Markus (2015) quotes a business owner from central Ukraine bewailing the “*myriad*” of agencies that would routinely swoop on his business to extract as much as possible in bribes, and enumerating: “*fire safety, sanitation, quality control, social funds, tax police – there aren’t enough fingers on both hands to count them!*”<sup>60</sup>. The sheer volume of the bribes demanded by these agencies, and the haphazard fashion in which their visits took place, was enough to severely incapacitate many firms by disrupting their cash flow and hindering their ability to conduct normal business, imperilling their property rights in the process. Let us recall that in the 2007 business survey designed by Stanislav Markus which asked Ukrainian firms to evaluate the impact of various threats emanating from state officials on their business operations, “*Illegal inspections by regulatory agencies*” was ranked as the second highest, with an average of 2.29 on a scale of 1 – 4<sup>61</sup>. Furthermore, the character of the threat posed by regulatory agencies as described here – overlapping, uncoordinated attacks by different groups of officials – strongly suggests that this is an area in which *decentralized* predation is rife. Not only do we have at work here some of the classic principal-agent problems discussed in the literature on corruption, but predatory behaviour *between* different state agents is uncoordinated and leads to an excessive bribe and rent-seeking burden for the firms affected.

## The state of Agent Predation in Regulatory Agencies in Post Maidan Ukraine

In the aftermath of the Maidan Revolution in 2014, one of the key areas of the state apparatus that was immediately identified as in desperate need of reform was the abundance of state regulatory agencies at work in the country, many of which appeared to exist for no other reason than to enrich the legions

---

<sup>58</sup> Dubrovskiy (2015), *op cit*.

<sup>59</sup> Anders Aslund, “How Ukraine became a Market Economy and a Democracy”, Washington D.C., Peterson Institute (2009), pg. 94

<sup>60</sup> Owner of a pharmacy in central Ukraine quoted in Markus (2015), pg. 66

<sup>61</sup> See page 8 above, and Markus (2015) pg. 76

of bureaucrats they were stuffed with<sup>62</sup>. A representative of the Ukrainian State Fiscal Service was quoted as commenting that the government had has “70 different bodies with licensing authority, including 40 with the power to shut down a business”<sup>63</sup>, and Volodymyr Hroysman, who would become Prime Minister in 2016, called for 20 of Ukraine’s “80 different inspectorates, controlling organs, and control departments in ministries”<sup>64</sup> to be shut down. It is not just Ukraine’s unhappy story of rapacious regulatory agencies but also international experience and conventional wisdom that informs their perspective; a 2009 study by the World Bank argued that excessive regulation and excess of regulatory agencies could be correlated with increased corruption<sup>65</sup>. Since this diagnosis was made in 2014, considerable progress has been made towards closing off opportunities for regulatory agencies to predate on businesses by shutting down superfluous inspectorates and regulatory agencies; a number of the most ineffective and corruption-prone regulatory agencies have been abolished, such as the Price Inspectorate, the Sanitary Inspectorate, the Traffic Police Inspectorate and the Real Estate Registration Agency<sup>66</sup>. Furthermore, legislative deregulation of the business environment has advanced significantly, with thousands of mandatory administrative services and procedures for Ukrainian businesses have been cancelled<sup>67</sup>.

Nevertheless, agent predation from state regulatory agencies demonstrably persists, and remains one of the greatest threats to the development of Ukrainian firms. In a blog post from April 2017 entitled “You have a business? Then we’re coming for you!” (author’s translation) Irina Lekh, founder and director of “Porada”, a business association based in Zaporizhia in South East Ukraine which represents companies from across the region, excoriatingly describes the range of agencies that Zaporizhian business report being harassed by; the State Ecological Inspectorate, for example, instead of inspecting the numerous factories and industrial complexes around the region (which are notorious for pumping pollutants and toxic substances into local rivers and lakes), target restaurants for their inspections, looking for opportunities to harass firms that lack the requisite permits for different types of emissions the disposal of waste products<sup>68</sup>. Meanwhile, the “State Agency for Consumer Protection”, on the basis of complaints submitted by citizens who do not exist, have been carrying out unannounced, unauthorized inspections (note the decentralized component here; there is a lack of coordination

---

<sup>62</sup> Åslund, “Ukraine: What Went Wrong and How to Fix It” (2015), *op. cit.* pgs. 135-137

<sup>63</sup> Stecklow, Piper, and Akymenko, “Here’s How Scams and Shakedown Brought Ukraine’s Economy to Its Knees” (2014), *op. cit.*

<sup>64</sup> *Ibid.*

<sup>65</sup> D. Madani, “Restrictive regulation is positively correlated to corruption,” *World Bank*, 12.10.2009, (<http://blogs.worldbank.org/psd/restrictive-regulation-is-positively-correlated-to-corruption>)

<sup>66</sup> Lough and Dubrovskiy (2018), pg. 20

<sup>67</sup> IERPC, Ukraine’s Fight Against Corruption: The Economic Front, *op. cit.* pg. 58

<sup>68</sup> Irina Lekh, “У Вас еще есть бизнес? Тогда мы идем к Вам!”, 28.04.2017 (<http://irinaleh.com.ua/u-vas-eshhe-est-biznes-togda-myi-idem-k-vam/>), accessed March 2019

among different agencies and their supervising central bodies) with up to 8 inspectors involved at a time!<sup>69</sup> Strikingly, Lekh has much to say about local government bodies' bullying and extractive activity in their regulatory capacities; she recounts how an inspection campaign was launched regarding businesses' development of public space ("инспекция по благоустройству"), supposedly to counter unlicensed street trading. Instead, the authorities sent hundreds of letters to those firms whose outdoor signage and advertising were a couple of inches longer than the statutory size, threatening to demolish the firms' property if they did not "come to an agreement" (i.e. pay a bribe).

The quarterly reports of the Business Ombudsman of Ukraine are replete with incidences of decentralized state regulatory agencies abusing their discretionary powers in order to, at best, siphon off bribes from entrepreneurs and, in some cases, jeopardise the very economic future of a firm by denying them essential permits and the freedom to operate until informal payments are made. On the small-scale end of the spectrum would be a case from June 2018 of a car-wash company from Odesa which had submitted to their Odesa branch of the State Architectural and Construction Inspection of Ukraine (DABI) notification of their intention to start construction of a car wash facility – permission from this body was essential for him to be able to start construction<sup>70</sup>. Although the procedure for obtaining such a permit is supposed to take less than 24 hours according to the law, the DABI took a month to respond, eventually sending the documents back and refusing the application because the applicant had missed a letter "i" in his spelling of the word "pavilion"<sup>71</sup>. However, the entrepreneur reports that an intermediary offered to "speed up the process" for him – i.e. pay a bribe – which the firm owner refused, turning to the Business Ombudsman instead. A more serious case from the BOCU's reports concerns the same regulatory agency, DABI, in the same region, Odesa; a developer who had built a parking lot for his sales operations in 2016 had spent two years seeking permission from DABI to register the facility, meeting continually with refusals<sup>72</sup>. The agency even ignored a ruling by the Odesa administrative court in the complaint's favour! The account of the Business Ombudsman investigator clearly indicates that the pressures building up for the firm as a result of the agency's delays and refusal to grant permission (mostly likely holding out for an informal payment) were affecting the firm's ability to run properly and to make a profit: *"At the same, time the company was suffering losses. One could not reimburse building costs because the facility did not work. In addition, it was necessary to pay for the lease of the territory..."*<sup>73</sup>. The firm finally turned to the Business Ombudsman *"When it*

---

<sup>69</sup> Ibid.

<sup>70</sup> Business Ombudsman of Ukraine Quarterly Report, Quarter III, 2018, pg. 81 ([https://boi.org.ua/media/uploads/q32018/iii\\_2018\\_en.pdf](https://boi.org.ua/media/uploads/q32018/iii_2018_en.pdf)), accessed June 2019

<sup>71</sup> Ibid.

<sup>72</sup> Business Ombudsman of Ukraine, Annual Report 2018, pg. 53-54 ([https://boi.org.ua/media/uploads/annual2018/annual\\_report\\_2018\\_en.pdf](https://boi.org.ua/media/uploads/annual2018/annual_report_2018_en.pdf)), accessed June 2019

<sup>73</sup> ibid

*seemed that it was impossible to defend its legal rights*”; clearly, this is a case of the obstinacy of the regulatory agency translating a bureaucratic delay into a potential threat to property rights.

Lekh’s singling out of the local authorities for their predatory role in regulation and inspection of business is also reflected in the Business Ombudsman’s case reports, which frequently detail the attempts of local agents to pressure firms into informal payments using their regulatory responsibilities. One case is illustrative of the decentralized dynamics involved, which concerns a company that specializes in paint coats for metal products<sup>74</sup>. For literally *years*, the Kyiv City State’s Local Administration’s Department of Ecology and Natural Resources refused to grant a pollutant emission permit to the firm, continuously raising objections that in the Business Ombudsman Investigator’s view were ungrounded – such unfathomably long delays and obstructive behaviour is an unmistakable prelude to the inevitable extraction of a bribe or other form of informal payment. Eventually, the problem was resolved when the Business Ombudsman raised the matter with Kyiv Mayor Vitaliy Klitshko. Note that this is a classic case of attempted *decentralized* predation, which happened without the consent of the state principal and was plainly contrary to the interests of the agent’s boss – in this case, the mayor of Kyiv - who has no interest in the trade of a local tax-paying company being disrupted, and moved swiftly to resolve the issue once it was brought to his attention. This is illustrative of one of Markus (2015)’s arguments about agent predation, that it occurs even when it is contrary to the stated policy objectives of the state principal (or even the senior local authority)<sup>75</sup>. We shall address more fully the question of predatory and rent-seeking proclivities in the regulatory functions of local authorities in the section on divergences in regulatory compliance between local and national authorities (page 31).

We can turn to the raw data from the Business Ombudsman Council’s files of complaints up to March 2019 to examine how large the threat from regulatory agencies and inspectorates looms in the complaints submitted by firms over the last five years. Complaints regarding “state regulators” account for 409 of the 5190 complaints handled during this period, accounting for almost 8% of the total. This makes state regulators the third most complained about type of state agency, behind the State Fiscal Service and Law Enforcement Bodies. The table below sets out the most prominent offenders among decentralized Ukrainian state regulators and their agents, accounting for 174 cases:

---

<sup>74</sup> Business Ombudsman of Ukraine, “Systemic Report: Challenges for Government and Business for Dealing with Local Government”, February 2017, pg. 26 ([https://boi.org.ua/media/uploads/systemic\\_report\\_-\\_february\\_2017/system\\_01\\_en.pdf](https://boi.org.ua/media/uploads/systemic_report_-_february_2017/system_01_en.pdf)), accessed June 2019

<sup>75</sup> Markus (2015), pg. 151

Type of State Agency	No. of Cases Submitted to Business Ombudsman of Ukraine
Regional Departments of State Service on Labour Issues	26
Regional Departments of Antimonopoly of Ukraine	9
Regional Departments of State Service of Ukraine on Food Safety and Consumer Protection	16
Regional Departments of State Service of Ukraine on Geodesy, Cartography and Cadastre	41
Regional Departments of State Ecological Inspection of Ukraine	16
Regional Departments of State Architectural and Construction Inspectorate of Ukraine (DABI)	38
Regional Departments of State Property Fund of Ukraine	5
Regional Departments of State Service of Ukraine for Transport Safety	8
Other Miscellaneous Branches of State Regulatory Agencies	16

It should be noted that here we have treated all cases involving a regional branch of a state regulatory agency as “decentralized”, as opposed to complainees which in the BOCU’s database are referred to as a central state agency, such as “Antimonopoly Committee of Ukraine”. This is admittedly a very imperfect way of tracking which cases might involve *decentralized predation* as opposed to corruption/expropriation from a central body – after all, it’s perfectly plausible that high-ranking agents of central state agencies could be engaged in decentralized predation of their own! However, it is the closest that the Business Ombudsman data come to drawing a distinction between centralized and decentralized agents. The data here attest to the significance of state regulatory bodies and inspectorates in Ukraine as a potential vehicle for agent predation, as reflected in the complaints submitted by Ukrainian firms (remember, the Business Ombudsman is chiefly seen as a point of call for firms who have exhausted all other legal means of redress and who suspect that they are facing the threat of corruption/rent seeking by public officials). Yet it appears that the problem is not so much restricted to decentralized regulatory agents as endemic to Ukraine’s regulatory infrastructure as a

whole, including central state bodies; after all, of the 409 cases concerning regulatory agencies, over half were the result of behaviour not of decentralized, regional branches of these agencies but the central head agency itself. In following section, we will attempt to “zoom in” on the unequivocally *localized* actions of local authorities in Ukraine by examining their role in the regulatory environment for firms operating on their territory, and the threats of decentralized agent predation that are associated with this activity.

### Section 3. Divergences in Regulatory Compliance and Commitments to Reforms Between Local and Central Government: Space for Decentralized Predation?

In this section, we shall deal with the area of Ukraine’s economy that is arguably one of the rifest with unaccountable decentralized agent predation by local officials: the local business regulatory environment in cities, municipalities, and other sub-regional forms of local government. Large datasets such as those derived from the Business Environment and Enterprise Performance Survey (BEEPS) allow us to see, on the macro level, how firms across all regions and industries of Ukraine assess the impact of rent-seeking behaviour by local officials on their business. As we shall see, the latest survey results indicate that rent-seeking by local officials looms much larger in firms’ threat perceptions than centralized rent-seeking at the government or parliamentary level, and the impact of these local officials is related to their discretionary powers in the regulatory environment and its political economy. This is largely congruent with the evidence from semi-structured interviews and the analysis of the State Regulatory Service of Ukraine, which attests to the greater reluctance of municipal and regional authorities to implement the kind of regulatory and anti-corruption legislation that is lobbied for by Ukrainian civil society and international experts, and passed at the central government level.

## Analysis of Regulatory Rent Seeking at the Local Level – BEEPS Survey V and Evidence from Semi Structured Interviews

We are concerned with the discretionary powers and instruments that local Ukrainian bureaucrats have at their disposal to harass and threaten the property rights of Ukrainian firms, even in defiance of the self-declared policy priorities of the central sovereign (in this case, the president, the cabinet of ministers and to some extent the parliament). One area in which we might start looking for such instruments is the role of local authorities in establishing and influencing the local regulatory environment for firms operating in their territory. In terms of the scholarship, we are on familiar territory here; many researchers have examined the regulatory policy of local political regimes as an explanatory factor in the varying economic performance of different regimes within post-soviet states. Alexander Libman, in his study of the impact of Russian sub-national political regimes on regional economic growth, argues that *“the most obvious impact of sub- national governments is associated with the stability of the business environment, business regulation, and the protection of property rights”*, since *“Even if the country is centralized, sub-national governments have, either formally or informally, a large influence on how businesses are regulated in a particular region (i.e., licensing and on-site monitoring of business activities)...”*<sup>76</sup>. Ukraine is no different in this respect; the executive councils of local authorities have considerable discretion when it comes to the regulation of the business climate. As well as determining regulations governing the leasing of land and property that is under the council’s control, Ukrainian local authorities have, in the words of a report by Transparency International, *“vast powers pertaining to entrepreneurship”*, which include the approval of outdoor seating for restaurants and cafes, the placement of signs and advertising, and deciding whether construction companies are required to invest themselves in public infrastructure projects<sup>77</sup>. As we are investigating the role of local authorities and officials in threats to firms’ property rights, it makes sense to consider how local authorities’ supervisory and regulatory functions could adversely impact the business climate.

Transparency International’s reports, and the testimony of my semi-structured interview with a representative of the TI office in Ukraine, identify local regulatory control of business as one of the key

---

<sup>76</sup> Alexander Libman, “Democracy, size of bureaucracy, and economic growth: evidence from Russian regions”, *Empirical Economics*, December 2012, Volume 43, Issue 3, pp 1321–1352, pg. 1324

<sup>77</sup> Transparency International Ukraine, “Analytical Report: Ways to Ensure Investment Sector Transparency in Cities”, August 2018, pg. 19 ([https://ti-ukraine.org/wp-content/uploads/2018/11/Analitchnyj-zvit-pro-investytsijnu-sferu\\_web\\_eng.pdf](https://ti-ukraine.org/wp-content/uploads/2018/11/Analitchnyj-zvit-pro-investytsijnu-sferu_web_eng.pdf))

areas in which predatory agents are able to manipulate the local legislative framework, often in breach of national law, in order to target firms under the pretext of regulatory oversight. As my respondent from the TI office explained, this can be done through the passing of regulatory acts at the local level by town councils (miskrada) and their executive organs (vykonkom). For example, a local council that has been captured by private interests might pass a local regulatory act establishing new criteria that must be met by any company that leases municipal land or property (buildings must conform to particular standards, applications must be submitted and approval sought etc.). Generally speaking, regulatory acts relating to entrepreneurship that are passed by executive councils are developed and promulgated in an extremely opaque way, with minimal public consultation and advance notice, which makes it very easy for business owners to learn about these new act for the first time only after being informed that they are in violation of it. Thus, the companies leasing municipal land or property that are presented with news that they are in violation of the recently passed act are placed in a vulnerable position; they can be exposed to the rent-seeking and predatory instincts of local officials, who might exact hefty bribes for “smoothing over” the firms legal troubles, or simply use them as cause for cancelling the firm’s lease agreement with the local authority, perhaps in favour of another firm associated with the official.

Markus’ mention of Ukrainian councils’ local regulatory and legislative powers is instructive, but mainly anecdotal and in need of more extensive analysis. It raises the question: how great of a threat to their business operations do firms regard the misuse of local authorities’ regulatory and executive instruments? To address this, we can refer to the results of the Business Environment and Enterprise Performance Survey (BEEPS), an economic survey run by the World Bank and European Bank for Reconstruction and Development that is carried out every few years across a number of developing countries, including Ukraine. The latest round of the survey was conducted in Ukraine in 2013-2014 and collected data from 1002<sup>78</sup> private enterprises from all regions of the country, and across a wide range of different industries. The survey data is collected through stratified random sampling from strata classed by size, industry, and geographic region<sup>79</sup>. In terms of the number of respondents, the geographic distribution of firms, and the coverage of different firm sizes (despite oversampling in favour of larger firms), the survey is one of the most comprehensive for Ukraine, and is regularly used as a barometer of business confidence and as a corruption perception index for the country’s private sector<sup>80</sup>, since many of the variables measured relate to corruption.

---

<sup>78</sup> Of which 513 were “small” enterprises of between 5 and 10 employees, 346 were “medium sized” (20-99 employees) and 143 were “large” (over 100 employees)

<sup>79</sup> <http://www.enterprisesurveys.org/Methodology/>

<sup>80</sup> See, for example: Elena Denisova-Schmidt, Martin Huber, “Regional Differences in Perceived

The 2014 round of BEEPS asks a question that, as Athanasouli (2016) points out<sup>81</sup>, is specifically targeted at identifying rent-seeking practices in the regulatory space at different levels of government. The question asks firms to assess the comparative impact on their business of “private payments” or gifts in order to alter the content of government decrees and to sway votes to (a) members of parliament, (b) government officials and (c) local or regional government officials. Considering that option (c) focuses on *local* and *regional* officials, we may reasonably infer that the “government officials” in option (b) refers to other various state actors from the *central* government level (which might include, for example, the personnel of ministries or government agencies), so as to be distinct from (c). The “impact on business” variable is measured a likert scale of 1-4, where 1 is “no impact” and 5 is “decisive impact”. The results, shown below, indicate that Ukrainian firms on average attribute a higher impact on their operations to officials from “local or regional government”, with a mean score of 2.091, compared to 1.783 for central government officials and 1.655 for parliamentarians.

To what extent have the following practices had a direct impact on this establishment?	Private Payments/gifts or other benefits to Parliamentarians (N = 679)	Private payments/gifts or other benefits to Government officials to affect the content of government decrees (N = 682)	Private payments/gifts or other benefits to local or regional government officials to affect their votes or content of government decrees (N = 770)
1 - No impact	62.0%	58.1%	45.6%
2 - Minor Impact	16.1%	15.0%	16.9%
3 - Moderate Impact	17.7%	19.5%	24.3%
4 - Major Impact	2.9%	5.6%	9.4%
5 - Decisive Impact	1.3%	1.9%	3.9%
Average Score	1.655	1.783	2.091

The BEEPS data are corroborated by data from another separate Ukrainian business survey, conducted in 2013 by Socioinform for a research project by Lviv’s Ivan Franko National University and the University of St. Gallen, and used by Denisova-Schmidt and Huber (2014) in their analysis of regional variation in perceptions of corruption among Ukrainian firms<sup>82</sup>. The survey sample was stratified by geography and firm size; the geographical distribution of the companies was almost precisely even across Ukraine’s 24 oblasts (25 firms selected from each oblast), presumably because the focus of the

---

*Corruption among Ukrainian Firms*”, Economics Working Paper Series 1407, University of St. Gallen, School of Economics and Political Science, April 2014 (<http://ux-tauri.unisg.ch/RePEc/usg/econwp/EWP-1407.pdf>)

<sup>81</sup> Daphne Athanasouli, *Corruption in Ukraine in Comparative Perspective* in Hale and Orttung (eds) *Beyond the Maidan: Comparative Perspectives on Advancing Reform in Ukraine* (2016), pg. 88

<sup>82</sup> Denisova-Schmidt, Huber, “Regional Differences in Perceived Corruption among Ukrainian Firms” (2014), *op. cit.* pg. 5

study was variation between oblasts. Although the sample underrepresents micro-businesses, which account for 82% of businesses in Ukraine<sup>83</sup>, since businesses classed as “very small” (below 20 employees) were not included – and these types of firms are arguably the most affected by the practices described in this section - it still represents a useful cross-section of the Ukrainian private sphere. This survey also asked firms to assess how often they encountered “informal practices” and corruption when dealing with a variety of different state agencies, institutions and officials at different levels of government. As with the BEEPS, we can use these results to gauge how the threat of rent-seeking varies, in the eyes of Ukrainian firms, between more local and more central state institutions.

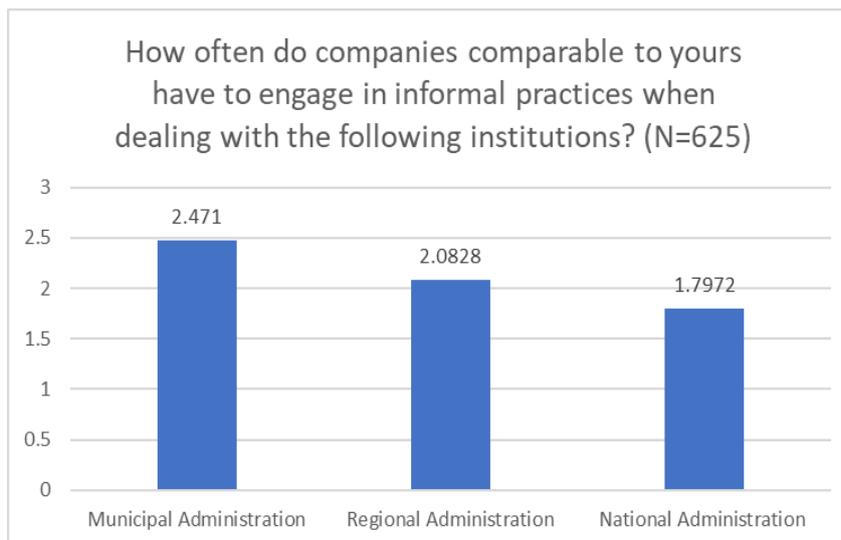
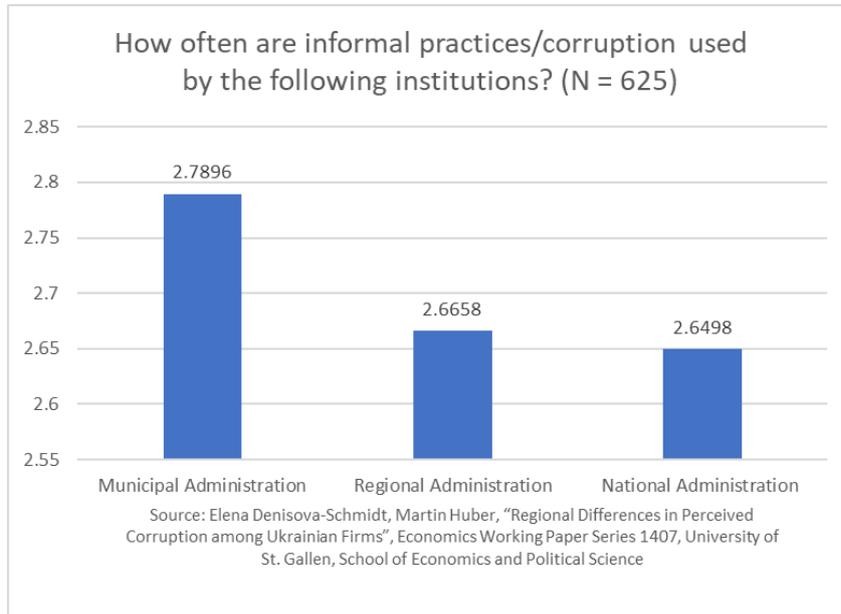
In fact, the survey questions discussed by Denisova-Schmidt and Huber are likely to have a higher validity for the variable *threat of rent-seeking/corrupt activity from central or local authority*, since the wording of the questions appear to control for the frequency with which firms have to interact with the authorities in question. Whereas the relevant BEEPS question asks firms to score the “*impact of these practices on your establishment*”, and thus respondents might be inclined to assign a worse score to local municipalities and officials chiefly because they have to deal with these institutions more frequently, even if the level of corruption of local institutions is the same as those of the central state, the survey used by Denisova-Schmidt and Huber merely ask *how often* each institution engages in corruption. This question seeks to ascertain the comparative tendencies of different authorities towards rent-seeking and the practices being discussed here.

As we can see (below), the survey data once again indicate that the Ukrainian firms interviewed on average regarded their local councils/municipalities as more prone to “informal practices” or corruption than authorities representing the national or central administration; municipal administrations were scored 2.7896 on the frequency with which they engage in these practices (where 1 means “never” and 4 “systematically”), compared to 2.6498 for the national administration. Interestingly, the difference in score between “regional administrations” (referring to rayon and/or oblast councils and administrative councils) and the national administration on this point was shown to be negligible. We might speculate on why this might be the case, considering the arguments already put forward; although officials and political stakeholders in oblast and rayon administrations are certainly well supplied with rent-seeking opportunities in their interactions with business, especially concerning the disposal of land and investments/infrastructure funding, they are typically not as involved in setting the regulatory environment which firms must operate in as municipal councils are. Thus, it might well be the case that for the average business, there are more areas in which encounters with the local council’s regulatory

---

<sup>83</sup> Vesta Malolitneva, “Reduction of Regulatory Burden on Small and Medium Enterprises: European Experience”, *VoxUkraine*, 23.11.2015 (<https://voxukraine.org/en/reduction-of-regulatory-burden-on-small-and-medium-enterprises-european-experience/>), accessed May 2019

system could carry risks – permits that need to be obtained and renewed, protean regulatory acts that are issued and then regularly rephrased, etc – and this is reflected in the survey results.



These data reflect the experience of Ukrainian firms for whom the threat of rent seeking from local authorities wielding significant influence over the regulatory environment looms larger than the threat of predatory officials from Kyiv or the Verkhovna Rada. This is in spite of the fact that, in Ukraine, local authorities (whether at the oblast, rayon, or selo level) actually have very limited powers in areas that we would expect to be most important for entrepreneurship and to drive concerted lobbying from the private enterprise side as well as rent-seeking from the government side; namely, control over tax rates and public investment. Even the recent decentralization reform has not yet changed the fact that most

regional public investment in Ukraine is channelled through centralized organs such as the State Fund for Regional Development, and municipalities have no capacity for borrowing themselves for access to external investment<sup>84</sup> – this means that local firms have limited opportunities for petitioning local authorities for subsidies. Likewise, entrepreneurs in Ukraine have little to gain from lobbying their local authorities for preferential taxes, since despite changes in legislation to allow for local councils to set (within limits) their own rates on income tax payments for the self employed and property and land tax<sup>85</sup>, they do not have the power to introduce significant tax breaks for firms on their territory in order to stimulate investment and entrepreneurship – a fact that was confirmed in semi-structured interviews with representatives of Ukrainian business associations and senior officials from Boryspil Rayon administration<sup>86</sup>. Instead, most of the rent-seeking and informal payments that local authorities extract derive from the powers outlined above that allow them to influence the business climate; allocation of leases and permission for development on municipal land, other miscellaneous regulatory powers such as those relating to advertisement, and the granting of public tenders.

Evidence from semi-structured interviews highlights the rent-seeking and corruption risks that these regulatory powers can pose to local Ukrainian businesses. These findings can lend updated empirical weight to the rather off-hand observation by a World Bank report on the economic climate of Ukraine from 2010 that Ukrainian firms face high entry barriers thanks to “*Institutional Barriers...that include a cumbersome system of licenses and permits for entry and operation*” which “*are prone to rent-seeking activities of regulatory agencies and local governments*”<sup>87</sup>. One respondent from the semi-structured interviews, Vira Nedzvedska, a legal expert from the East Europe Foundation who has worked on technical assistance projects aimed at deregulation and economic development, pointed to the example of locally set regulations for “outdoor advertisements”:

*“For small and micro businesses, it’s a huge problem because in Ukraine we have very complicated regulations on outdoor advertisement – all kinds of rules for the information you display outside your shop to let people know that you conduct business here: these rules are used as an instrument to collect*

---

<sup>84</sup> OSCE, “Maintaining the Momentum of Decentralization in Ukraine”, OSCE Multi Level Governance Studies, 2018, pg. 228 ([https://read.oecd-ilibrary.org/urban-rural-and-regional-development/maintaining-the-momentum-of-decentralisation-in-ukraine\\_9789264301436-en#page1](https://read.oecd-ilibrary.org/urban-rural-and-regional-development/maintaining-the-momentum-of-decentralisation-in-ukraine_9789264301436-en#page1)), accessed April 2019

<sup>85</sup> T. Levitas. and J. Djikic, “Fiscal Decentralization and Local Government Finance Reform: 2014-2017”, SKL/SIDA Policy Brief, 2018, pg. 22 ([https://www.academia.edu/37642724/Fiscal\\_Decentralization\\_and\\_Local\\_Government\\_Finance\\_Reform\\_In\\_Ukraine\\_2014-17](https://www.academia.edu/37642724/Fiscal_Decentralization_and_Local_Government_Finance_Reform_In_Ukraine_2014-17)), accessed April 2019

<sup>86</sup> From Semi-structured interviews conducted in Kyiv in July 2019; at the respondents’ request, the names of specific individuals or organizations cited are confidential

<sup>87</sup> World Bank, “Ukraine: Country Economic Memorandum: Strategic Choices to Accelerate and Sustain Growth”, 31.08.2010, pg.36(<http://documents.worldbank.org/curated/en/200401468314067900/pdf/558950ESW0UA0p1Official0useOnly191.pdf>), accessed July 2019

*money, including bribes, but also to weed off businesses they are not “affiliated” with them [the local authorities]...to monopolize the market and punish rivals...”<sup>88</sup>*

Thus, the regulatory powers that local councils exercise even over a comparatively minor dimension of business activity such as advertising space can be used to apply pressure on firms that are not in some way “affiliated” with the local power-holders and their allies. When the laws governing advertising practices are unfathomably complicated or can be changed at will and without notice by local executive councils, violations are easily discovered in the practices of “undesirable” companies (such as the rivals of a company controlled by a member of the council); fines or bribes can then be extracted, and possibly even restrictions on that firm’s right to conduct their business. In this sense, we can see how such “selective application of impracticable rules” can very easily lead to threats to property rights following Markus’ arguments, since it will very soon become impossible to support one’s operations if the firm is constantly harassed by officials discovering violations in its outdoor advertising and depriving it not only of income (in the form of bribes and fines) but also crucial advertising space and, in some circumstances, the right to trade. Nedzvedska’s observations are corroborated by business survey data from USAID’s Leadership in Economic Governance Programme (LEV); according to their 2017 survey of over 2,000 Ukrainian firms, 12.8% of microbusinesses and 9.5% of small businesses surveyed described “Регулювання зовнішньої реклам” (regulation of outdoor advertising) as a “significant problem” in their business environment<sup>89</sup>. Other elements of the business climate in which local authorities play a decisive role loom even larger in firms’ assessment of regulatory difficulties; “Регулювання землекористування” (land-use regulation) was regarded by micro, small and medium sized firms as equally problematic, with at least 30% of each group describing them as a serious problem<sup>90</sup>. Interestingly, the panel of 84 business experts from Ukraine’s 25 regions surveyed as part of the LEV report ascribe an even higher comparative score to the difficulties of regulation of outdoor advertisement for small and medium sized businesses; on a Likert scale of 1 – 5, where 1 is “not a problem” and 5 is “significant problem”, the experts gave Регулювання зовнішньої реклам an average score of 2.38, higher than that given for “tax administration” (2.11) and acquiring licenses (1.76), although slightly lower than land regulation (2.94)<sup>91</sup>.

Other respondents from semi-structured interviews confirmed that all too frequently, the opaque and byzantine procedures governing business regulation in local councils make them prime areas for corrupt activity. Kadie Ward, senior governance advisor at the Partnership for Local Economic

---

<sup>88</sup> Interview conducted by the author with Vira Nedzvedska over Skype, May 2019

<sup>89</sup> Щорічна оцінка ділового клімату (ABCA, Annual Business Climate Assessment, 2016/2017), *op. cit.* pg. 246

<sup>90</sup> Щорічна оцінка ділового клімату (ABCA, Annual Business Climate Assessment, 2016/2017), *op. cit.* pg. 246

<sup>91</sup> Щорічна оцінка ділового клімату (ABCA, Annual Business Climate Assessment, 2016/2017), *op. cit.* pg. 208

Development and Democratic Governance Project (PLEDDG), a technical assistance project backed by Canadian donors which advises Ukrainian municipalities in Vinnytsia, Zaporizhia, Poltava and Ivano Frankivsk oblasts on economic development (including improvements to the local business climate) and governance reforms, described how *“the trend is really that the process is not transparent and the process changes...you spend lots of time preparing for a byelaw and the regulation and then by the time you’re ready the process has changed...”*. As a result, firms often find that the only way to save money and resources whilst protecting themselves from punitive measures and subsequent threats to property rights is to succumb and pay bribes in order to circumvent the issue of complying with the regulation. The bye-laws on business regulation developed and passed by local municipalities and the ambiguities of this procedure can therefore easily be adopted, in Ward’s words, as a *“tool of corruption”* in the hands of local politicians and officials<sup>92</sup>.

These corruption risks extend to local council’s management and leasing of municipal property and land. Another respondent, Yevhen Popov, an anti-corruption activist based in Odesa and a regional representative of the International Renaissance Foundation, knows more than most about some of the dubious practises of municipal councils that have been captured by private interests. Popov is the cocreator of an app, *Open Odesa*, developed with the support of UNDP, which allows users to monitor the activity of Odesa city council and to access information on the decisions made at meetings of the executive councils, the voting record and background of councillors, as well as the corruption risks present in any single council decision<sup>93</sup>. Popov emphasised that sessions of Odesa City Council are a crucial vehicle for maintaining vested interests’ financial control over the city and its environs, as it is here that decisions of great financial and political moment are made, especially those relating to the distribution of land and public contracts - all without due public scrutiny, democratic oversight, or any regard to potential violations of conflict of interest. The local authority’s control over lease agreements and sale of municipal land and property as well as the local regulatory environment is therefore readily wielded as an instrument to reward firms that are connected to the ruling clan(s) (in the case of Odesa, this consists of the mayor and his extensive network of business contacts who own most of the valuable assets in the city) with favourable leases, land and public contracts, whilst punishing firms that dare to compete with the clan’s interests or are politically obstreperous. As outlined above, these practices thrive through a combination of the lack of transparency in the local political process, which precludes proper investigation and the development of opposition, and the indifference of the public. Although the ruling party in Odesa has little to fear from exposure of their rampant crony capitalism in the city,

---

<sup>92</sup> Interview conducted by the author with Kadie Ward over Skype, July 2019

<sup>93</sup> UNDP Ukraine, “Open Odesa: Keeping Track of City Decisions”, 13.06.2019

(<https://undpukraine.exposure.co/open-odesa-keeping-track-of-city-decisions>), accessed June 2019

councils can be quite creative in their obfuscation and disguise of the allocation of finances and resources being directed during these sessions. Popov described, for example, how crucial information on financial transactions ordered by the city can be found as amendments or edits to documents that the council has supposedly already voted on:

*“it’s very interesting how they sometimes make corruption...the project of the decision [made by the council] is one document, and afterwards they vote on this document, but then add and edit lots of information...sometimes, for example, the decision will be about healthcare, but somehow when you look at the decision, you find them declaring “we need to sell this or that plot of land etc.”...”<sup>94</sup>*

Irina Lekh, founder of the regional business association “Porada”, provided a very similar assessment of the political reality in Zaporizhia, an industrialized south-eastern region of Ukraine where most of the key figures in the local municipalities represent the interests of the factories and businesses belonging to the most prominent oligarch of the region, Rinat Akhmetov. In an interview with the author, Lekh sketched out how these interests practically monopolize local politics in the city of Zaporizhia, and to some extent Zaporizhia oblast, with a factory in the city belonging to Akhmetov serving as the nucleus of this informal political group:

*“all decisions made in the city of Zaporozhia and Enerhodar - a town in Zaporozhia in which this political force [i.e. Akhmetov’s men] was victorious - are made in this factory...and the staff of the executive authorities are entirely made up of workers from SCM [Akhmetov’s company, which used to be based in Donetsk, but has now transferred to Mariupol in Zaporozhia]...the team of the executive council, the mayor’s deputies, the heads of departments, are all Akhmetov’s men and therefore all of the money that is spent by the Zaporizhia city budget is spent with a view to these political forces, all tenders go how they wish...”<sup>95</sup>*

The similarities with the situation in Odesa are immediately apparent. However, given that this research began by using Stanislav Markus’ work on threats to property rights in Ukraine as its reference point, it is important to point out the differences that are beginning to emerge between the evidence from our semi-structured interviews and Markus’ depiction of the predatory tendencies that plagued many local authorities across Ukraine in the post-Orange Revolution period. The testimony from experts and representatives of Ukrainian business associations suggests that local authorities in Ukraine, despite their important discretionary powers in determining the local business environment, rarely engage in wholesale, systematic extortion of firms on the scale documented in Markus’ work. The system of the

---

<sup>94</sup> Interview with Yevhen Popov in Kyiv, July 2019

<sup>95</sup> Interview with Irina Lekh via Skype, June 2019

*Smotryashchy*, whereby the regional governor's representative would collect tithes from local companies in return for not making it impossible for them to conduct their business, was fairly typical of the Yanukovich period, but has largely disappeared now. Judging from semi-structured interviews with business association representatives, this might be due to the fact that since the Euromaidan revolution of 2014 and the election of successive (at least rhetorically) Europe-orientated, reform-minded and (not just rhetorically) bankrupt governments, such overt, systematic threats to property rights could not be tolerated even in Ukraine's regions by a central sovereign that had come to power on a tide of anti-corruption sentiment and was in the process of appealing to the IMF for loans in return for meeting conditionalities on fighting corruption.

Instead, it appears that one of the main obstacles for the development of free enterprise in many of Ukraine's localities today is not so much flagrant predation *per se* as the local elite's monopolization of all or most of the most valuable assets on the territory (chiefly land, property and factories as well as other private assets), and the consolidation of these assets and income streams against threats from competition and/or civic oversight through their control over the local political process. Of course, one could argue that to some extent this is a false dichotomy; after all, many of the "disorganized predators" category designated by Markus were extorting and threatening the property rights of firms fully in the knowledge that entities under their own control would be the beneficiary were their rivals to face bankruptcy or expropriation of some kind. Nevertheless, if the threat of sustained siphoning off of the firm's income at the expense of predatory bureaucrats is becoming far less of a threat in the eyes of Ukrainian enterprises in the last five years than the monopolization of the local economy by its political elites, this is still a qualitative distinction worth making. Some of the experts and business owners interviewed were hesitant to describe the new status quo as at least more stable for firm owners who are prepared to keep their heads down and refrain from challenging the ruling political faction's business interests – which is what we might assume if we were seeking a silver lining in these developments. Yevhen Popov, the anticorruption activist from Odesa and designer of the *Open Odesa* app, agreed that firms would generally consider their property rights secure from infringements by local political actors and officials, so long as they themselves were not a competitive threat to the ruling elite's operations or interfered with their interests by, for example, seeking to develop or lease the same valuable land plots<sup>96</sup>.

Irina Lekh, who has been campaigning and representing the interests of small and medium sized businesses in Zaporizhia oblast for over a decade and who was an active participant in Zaporizhia's own "Maidan" which ejected the former *Smotryashchy* in the region, was more ambivalent about the

---

<sup>96</sup> Interview with Yevhen Popov in Kyiv, July 2019

current threats to property and income rights emanating from local authorities. In one excoriating blog post from 2016, she wrote that “one *Smotryashchy* has been replaced by another”, with the main difference being that whilst the previous rent-seeker-in-chief had preferred to operate in the city of Zaporizhia itself and had constructed for himself a local base for “wringing (*otzhatom*) business premises”, the new *Smotryashchy* opted to “save on overhead” by staying put in the Oblast State Administration building. Nevertheless, her commentary on the activities of the new post-Maidan authorities in Zaporizhia does suggest an alternate approach to that of the previous *Smotryashchy* – a slight shift from overt collection of rents from a broad cross section of different local businesses (under threat of expropriation) to exploiting the administrative and legal powers of the local authority, especially when it comes to state-owned property and enterprises, in order to monopolize several profitable local markets in select fields; medicine, transport, construction, and transportation<sup>97</sup>. For example, after illegally forming a “working group” out of the administration’s regulatory and supervisory authorities, the *Smotryashchy* set out to conduct inspections of medical facilities and companies providing medical services within the local authority’s territory. He was able to put pressure on the head physicians of these medical facilities, threatening them with being placed on the “black list” (i.e. being fired), to drive out their previous tenants and free up space for the *Smoytrashchy*’s own companies to occupy the facilities. These resources allowed him to arrogate to himself and entities under his control the lion’s share of all procurement contracts for medical equipment, as well as local monopolies in the funeral business and medical forensics (*Sudmedexpertiza*)<sup>98</sup>. Likewise, in the construction market, Lekh reports that the majority of building contracts are won by firms with links to a shadow company listed in Cyprus offering collateral of 3 million hryvnia<sup>99</sup>. The new *Smotryashchy* also ventured into the public transportation sector; in complete violation of national economic competition rules, he drew on the public budget to form a “communal public transport enterprise” (in Ukraine the misleading term “communal enterprise” normally refers to a state-owned company with little or no “communal” dimension), which rapidly gobbled up public tenders for passenger transportation, evicting long-established players from the market. Unsurprisingly, the financial records and beneficiaries of this communal enterprise were kept hidden from the public – as with the inner workings of municipal councils and their decision-making process discussed above, financial opacity and lack of public scrutiny allows this concentration of assets and market power to go unopposed.

---

<sup>97</sup> Irina Lekh, “Три года с начала Запорожского Майдана: что изменилось?” (“Three years since the beginning of the Zaporizhian Maidan: what has changed?”), 30.10.2016 (<http://irinaleh.com.ua/tri-goda-s-nachala-zaporozhskogo-maydana-chto-izmenilos/>, accessed January 2019)

<sup>98</sup> Ibid

<sup>99</sup> Lekh, “Три года с начала Запорожского Майдана: что изменилось?”, *op. cit.*

Undoubtedly, in the final analysis this kind of behaviour corresponds to the category of the “disorganized predator” as described by Markus – i.e. a local political actor who abuses his discretionary powers in order to extract rents and in some cases threaten the property rights of firms. In an interview with the author, Lekh concluded that the situation for private firms in Zaporizhia was “about the same” as it had been in the Yanukovich period, only the methods had changed, and the damage was probably less widespread, since *“Of course, during the Yanukovich period, more business owners suffered...today they seemly steal from businesses in a different way, not so impudently (нагло)...they don’t come up to you and say “give me your business”, but simply don’t give you the opportunity to work...”*<sup>100</sup>.

## Divergences in Commitment to the Reform Process Between Central and Local Government

Why do Ukrainian firms consider themselves more vulnerable to predatory and rent-seeking behaviour from local authorities than from central state actors, even when surveys control for the fact that they encounter local authorities more often? One explanation may lie in the fact that local executive councils in Ukraine have been relatively insulated from the reform agenda that has been pursued and implemented (albeit unevenly) at the central government level in Kyiv over the last few years. The testimony from experts in semi-structured interviews, as well as data from other reports, suggest that local authorities in Ukraine are under much less pressure to reform their administrative structures and governance practices in line with the central government and civil society’s legislative efforts to combat corruption and defend property rights through institutional reform and transparent deregulation of the business environment. Since 2014, the Ukrainian government, assisted by a host of international donors and civil society organizations, has been generating reams of anti-corruption legislation and adopting new frameworks and standards for public administration covering almost every aspect of governance in the country; new anti-corruption institutions have been established or are about to be established, tax and VAT administration systems have been reformed, amendments made to the legislative framework of the judicial system<sup>101</sup>, and a strategy for full scale reform of the civil service based on European best practices has been adopted. Underpinning many of these reforms are the principles of openness and transparency, reflecting the findings of anti-corruption research and the viewpoint of many of the international organizations at work in Ukraine (IMF, World Bank, EBRD, UNDP, and so on)

---

<sup>100</sup> Interview with Irina Lekh via Skype, June 2019

<sup>101</sup> OSCE, “Maintaining the Momentum of Decentralization in Ukraine” (2018), page 9

that institutions and public servants are more resistant to corruption when their work and budgets are transparent and open to the public.

Exactly how effective these measures have been is of course debatable and many thousands of pages of research have already been devoted to answering that question, but there can be little doubt that in spite of tremendous resistance from vested interests, many of the reforms implemented by the Ukrainian government have at least introduced new constraints on public officials who might be inclined to seek profit through rent-seeking, and closed off some of the opportunities for corrupt activity. An outstanding example of this would be the launch of ProZorro, the online platform for public procurement which state bodies are mandated to use when contracting for goods and services worth over 200,000 UAH and for works over 1.5 million UAH; in their assessment of the economic impact of Ukraine's anti-corruption reforms, Kyiv's Institute for Economic Research and Policy Consulting estimate the savings made from the use of ProZorro for public tenders since 2015 at 40 billion UAH<sup>102</sup>. Likewise, Ukraine's civil service reform, inaugurated by "The Law on Civil Service" which was passed by parliament in 2016, has been positively received by international observers and is credited with beginning to "*establish a new culture of administration*"<sup>103</sup> by introducing more transparent, merit-based recruitment procedures for civil service positions, raising salaries and limiting discretionary components of civil service compensation.

One of the most crucial areas of the reform process, highly pertinent to this research topic, is deregulation – something that Ukrainian businesses and foreign investors have long been clamouring for and which successive governments have sought to address<sup>104</sup>. The reason it is pertinent is that sensible deregulation of the business environment, filtering down through every layer of the Ukrainian economy, might reasonably be supposed to be the natural antidote to the very problems we have been discussing in the previous section: that is, local councils and political actors wielding their controls over the regulatory environments as a weapon of rent-seeking or monopolization. If Ukrainian businesses run the risk of rent-seeking and predation every time they seek a permit to trade in a particular area or set up outdoor advertising or lease municipal property, one answer might be to reduce the number of hurdles that both central and local authorities can place in front of firms and cut through the bureaucratic procedures and controls that inhibit growth and encourage corruption. Of course, cutting red tape is by no means automatically synonymous with constraining corruption, and some of the metrics most commonly used by economists and technocrats to assess progress in deregulation are

---

<sup>102</sup> Institute for Economic Research and Policy Consulting, "Ukraine's Fight Against Corruption: The Economic Front", 2018, page 8

<sup>103</sup> Lough and Dubrovskiy, *op. cit.* pg. 31

<sup>104</sup> IERPC, Ukraine's Fight Against Corruption: The Economic Front, *op. cit.* pg. 58

unreliable indicators of progress in fighting corruption – as Lough and Dubrovskiy point out, Ukraine improved its score on the World Bank’s “Doing Business” index by an impressive 23% under Yanukovych’s administration, but there is no evidence that this led to a comparable improvement in corruption perceptions amongst Ukrainian firms, and at the time the government itself had become notorious for its endemic corruption<sup>105</sup>. Nevertheless, one of the guiding principles of the government’s deregulation efforts is that a balanced, predictable and transparent regulatory system, properly enforced, will reduce the space for rent-seeking and corruption by state agencies. Since 2014, a number of institutions, think tanks and civil society organizations have been intensely engaged in the development of new regulations and regulatory policies. These include, to name just two, the State Regulatory Service (SRS) of Ukraine, a central executive body established in 2014 by the Ukrainian government to act as an intermediary between the government and the business community<sup>106</sup>, and the Better Regulation Delivery Office, an EU-funded think tank which advises the government on its regulatory policy and provides support for those starting a business. Such organizations not only assist in drafting new regulatory acts for consideration by parliament in consultation with business, but also apply a number of tests to draft legislation in order to check whether these regulations meet the right standards of efficiency, predictability and clarity, and that corruption risks are minimized.

Ukraine’s deregulation efforts and other changes to the system of interactions between private firms and state agencies should significantly limit the scope for corrupt practices, rent-seeking and predatory threats to firms’ property rights, so long as these reforms are properly implemented at every level of government and reach through to a critical mass of cities, municipalities and villages. Not only will the scope for abusing the discretionary powers bestowed on local authority and agency officials be reduced, but businesses themselves will find it easier to be compliant with rules that are straightforward, and less tempting to circumvent the regulatory system by making informal payments. As with Ukraine’s national anti-corruption policymaking, evaluating progress on the deregulation front is a difficult business, but there have undoubtedly been some important steps forward made in central government agencies. We have already noted that one of the first successes of the post-Maidan government was the liquidation of a number of shadowy government regulatory agencies and inspectorates (many of them dating to the soviet era) that seemed to exist for little other reason than the personal enrichment of their staff and directors.

---

<sup>105</sup> Lough and Dubrovskiy (2018), *op. cit.* pg. 20

<sup>106</sup> The State Regulatory Service of Ukraine, “Partnering with the businesses towards building effective economic policy”, 13.04.2017 ([http://www.drs.gov.ua/press-room/state-regulatory-service-ukraine-partnering-businesses-towards-building-effective-economic-policy/?print\\_page=true](http://www.drs.gov.ua/press-room/state-regulatory-service-ukraine-partnering-businesses-towards-building-effective-economic-policy/?print_page=true))

However, there is evidence to suggest that a substantial proportion of these regulations and reforms have not penetrated through to regional and local executive councils and administrations. It appears that, whilst the uptake of new regulations for the business environment that take into account corruption and rent-seeking risks is in full swing at the central government level, this momentum is not percolating through to the local business environments at a regional and municipal level. This was something that was stressed in the semi-structured interviews by Vira Nedzvedska, who has worked closely with local municipalities in assisting them with the drafting of regulatory policy and applying the tests that the State Regulatory Service recommends for proposed regulatory acts. According to her, there is a marked divergence between the speed and enthusiasm with which central government agencies and local governments adopt the principles of the new regulatory policy framework. Furthermore, noting that this divergence is a continuation from the Yanukovych period when deregulation did progress somewhat, she warned that increasingly local municipalities seem to be seizing the opportunities supposedly presented by the greater autonomy granted to self-governing communities to impose their own regulatory burdens on businesses under their purview:

*“even under Yanukovych, deregulation progressed, and the central government has abolished many regulations for small and medium sized businesses, but at the same time the problem was that local councils have not aligned their local regulations in line with the central government system and secondly, they even envisioned new regulation, this is the problem with decentralization reform, they wanted to have more influence over business and they adopted regulations which increased the burden on business...”<sup>107</sup>*

We shall see later that the claims made here about decentralization being the key factor leading to greater regulatory overreach by local authorities should be taken with a grain of salt. Suffice it to say, however, that Nedzvedska’s core claim – that the regulatory opportunism of local councils has not abated – seems to be supported by data published by the State Regulatory Service, which reported in 2019 that over the course of the past year (2018), the number of draft regulatory acts that local councils were issuing related to *“regulation of placement of temporary structures, small architectural forms [малих архітектурних форм], objects of trade, methods of advertising, signs, improvement of the condition of public areas [благоустрою територій], and rules for market trade”* increased dramatically, by 30% compared to 2017<sup>108</sup>. What most of these areas have in common is that they

---

<sup>107</sup> Interview conducted by the author with Vira Nedzvedska over Skype, May 2019

<sup>108</sup> State Regulatory Service of Ukraine, “Аналітичний звіт ДРС за 2018 рік” (Analytical Report of the SRS for the year 2018), Slide 20, February 2019 (<http://www.drs.gov.ua/press-room/analytychnyj-zvit-drs-za-2018-rik-2/>), accessed May 2019

relate to the physical space within which businesses conduct their trade, within the territory of local municipalities.

Now let us focus on the gap between central and local authorities in the implementation of regulatory policy. Data released for the year 2018 by the SRS, which monitors the implementation of regulatory reforms by central and local executive organs, can give us more insight into the kind of discrepancies that exist between different tiers of government. In their analytical report for the year 2018, the SRS highlighted that, whilst central government institutions are generally improving in their regard for and implementation of the recommendations and principles of regulatory policy being advocated by central, reform minded bodies (such as the SRS), progress on the local authority front is more uneven and, in many cases, stagnant. To begin with, the report examines how well regulatory agencies obey the “principle of predictability” i.e. that the regulatory acts passed by executive bodies are in line with their stated regulatory objectives for the year; this is vital for firms affected by local regulations as, to use the rather legalese phrasing of the SRS, it “allows business entities to carry out planning for their own activities and guarantees the right of businesses to participate in the regulatory activities of executive authorities” (my translation)<sup>109</sup>. Put simply, if the regulations produced by local and central bodies are in line with the publicly available and agreed up specifications of their policy plan, then businesses will be able to plan properly for complying with these regulations and will not be caught unawares. However, according to the SRS’s methodology, over the course of 2018, the number of regions in which the development of regulatory acts was carried out in accordance with their plans decreased, from 15 regions to 12, whilst the number of central regulatory agencies conforming with their plans doubled, from 8 to 15<sup>110</sup>. The report also highlights that the consistency of the plans themselves is lower for local authorities than for their central government counterparts; the authors claim (again, regrettably in rather stilted language) that “The level of consistency in approach to regulatory activity”<sup>111</sup> by local executive authorities has fallen, with 16 regional authorities introducing changes to their policies in 2018, compared to 10 in 2017. The implication of this is that regional and local executive councils in Ukraine are less willing or able to develop and pass regulations in a manner that is consistent with the central government’s own declared standards of regulatory policy. Indeed, according to another of the tests carried out by the SRS for their report, the level of “compliance with the state’s principles of regulatory policy” (i.e. the target standards that the SRS has set for new regulations) has been significantly lower for local authorities over the past three years than for central agencies. The SRS cites figures indicating that in 2018, for example, 20 regulatory acts were passed by

---

<sup>109</sup> Ibid, Slide 2

<sup>110</sup> Ibid.

<sup>111</sup> SRS, “Аналітичний звіт ДРС за 2018 рік” (Analytical Report of the SRS for the year 2018), *op. cit.* Slide 2

local councils even after they were submitted to the SRS for analysis and were not approved i.e. were passed without the consent of the SRS, whereas the figure for central state agencies in 2018 was 3<sup>112</sup>. Nevertheless, this does seem to be an area in which rapid progress is being achieved, since the number of acts being passed without SRS consent has halved for local authorities since 2016 (when 40 such acts were passed), and for central agencies the issuance of defiant acts has almost ceased, falling from 22 in 2016 to 3 in 2018.

The SRS's report draws attention to a similar trend of divergence between central state organs and local authorities when it comes to their commitment to consulting with the SRS in order to harmonize their regulatory strategy with that of the government's national agenda. For example, according to SRS data, local executive councils submitted only 16% of their draft regulatory acts to the State Regulatory Service for review<sup>113</sup>, although they are expected to send on all of their draft acts as part of the regulatory reform strategy. Unfortunately, it can hardly be said that the submission rate of councils is low because they are already perfectly capable of drafting sound regulatory acts without any help, since the SRS reports that in 91% of cases, they propose recommendations on how the acts can be improved, and in 6% of cases the documents submitted are either incomplete or contain violations of the law<sup>114</sup>. The unevenness of compliance across different regions is also striking - ranging from oblasts like Kirovohrad, which submitted a majority of their regulatory acts for review, to many oblasts which submitted barely any (including Odesa, Lviv, Zakarpathia and Zhytomyr oblasts). Although 99% of the regulatory acts proposed by municipal councils require being subjected to an "M Test" - a procedure based on EU best practices whereby a proposed regulation is analysed for the potential impact (both financial and in terms of corruption risk) it will have on small and medium sized businesses<sup>115</sup> - only in 64% of cases was an "M test" carried out.

Why is it that local authorities in Ukraine appear to be so less engaged with the processes of developing more business-friendly, corruption-resistant regulation than agencies that are directly controlled by the central government? A multitude of reasons could be suggested, certainly - including differing levels of access expertise and resources. However, there is also the factor of differing levels of constraints between central and local bodies. The crucial difference here is that, to put it bluntly, local authorities and municipalities can afford to simply ignore the recommendations of institutions such as the State Regulatory Service when it comes to drafting their own regulatory acts. As was confirmed by experts in

---

<sup>112</sup> SRS, "Аналітичний звіт ДРС за 2018 рік" (Analytical Report of the SRS for the year 2018), *op. cit*, Slide 3

<sup>113</sup> *Ibid*, Slide 13

<sup>114</sup> *ibid*

<sup>115</sup> American Chamber of Commerce in Ukraine, "Meeting with Ms. Kseniya Lyapina, Head of the State Regulatory Service of Ukraine", 23.11.2015 (<http://chamber.ua/en/Events/Event/1460>)

the semi-structured interviews, for ministries and central authorities it is mandatory to receive approval from the SRS before submitting their draft proposals for the Cabinet of Ministers' (the government's) agenda, whereas local authorities are under no such obligation. Technically, local councils are required by law to submit their draft regulatory acts to the SRS to be reviewed by the experts, but the majority of councils simply do not comply – and whilst the SRS is authorized to then provide recommendations on how the regulatory acts under review could be improved, the local councils are not obliged to follow these recommendations. To embed this in the terms of the theoretical literature on property rights discussed earlier in the literature review section, applied here to potential instruments of regulatory rent seeking rather than outright expropriation: the state *principal* (here represented by the central state agencies most closely subordinated to the principal) has placed constraints on its powers to pass regulatory acts by being obliged to submit them for approval to the SRS – which, whilst being a central executive body itself, has an excellent reputation as a watchdog for business interests in Ukraine and whose independence is protected by the support and cooperation of international donors – whereas local state *agents* (local councils and municipalities) have not been constrained in the same way. Of course, we are not equating the bureaucratic oversight of business regulations by the State Regulatory Service of Ukraine with the kind of deep institutional constraints on the principal that scores of political scientists have declared to be the foundation of secure property rights and of properly functioning democracies. Likewise, it would be unwarranted to assume *a priori* that all of the recommendations and guidance of expert councils such as the SRS represent constraints on predatory activity and an enhancement of the security of property rights. Nevertheless, the crucial point is that in both cases the central state principal is unable, or at least severely limited in its capacity to impose political and legal constraints on its regional and local agents – from this perspective, the analogy makes an important point about why rent-seeking regulatory policy might remain easier to pursue at the level of municipal councils than in centralized government ministries and agencies.

The reluctance (or incapacity, or indifference) of municipal authorities in Ukraine to respond the regulatory precepts being issued by the state principal is, according to some research, also mirrored in the indifference of many executive councils to the anti-corruption legislation that has been developed and promoted on the national level by a combination of government ministries, Ukrainian civil society and international donors. Such is the impression left by an analysis conducted by the Eidos Centre, a Kyiv think tank, as part of their “Transparent Councils” project<sup>116</sup>. The project investigated the local legislative activity of 56 city and regional local government councils, checking the implementation of

---

<sup>116</sup> Centre for Political Studies and Analysis, “Eidos”, 2016 Report, pg. 20 (<http://eidos.org.ua/wp-content/uploads/2017/07/10%D1%80%D0%BE%D0%BA%D1%96%D0%B2%D0%BE%D0%BD%D0%BB%D0%B0%D0%B9%D0%BD-%D0%B0%D0%BD%D0%B3%D0%BB.pdf>), accessed July 2019

anti-corruption legislation passed by the Rada into these councils' executive decisions and charters, up to a year and a half after this legislation was passed. According to the Eidos Centre's report, the results were *"more than sad... the overwhelming majority of officials at the local level ignored and did not implement them"*<sup>117</sup>; the implantation rate of the 21 anti-corruption laws being examined was a miserable 12%. Of course, isolated civil society and international development projects can help to correct this, but successes are sporadic, scattered across the country, and depend upon the goodwill and engaged cooperation of the local authorities concerned – in other words, they are highly decentralized, mirroring the decentralized character of the corrupt practises they seek to address. According to a representative of Transparency

International (TI) Ukraine interviewed by the researcher (TI Ukraine runs a large-scale project, "Transparent Cities", aimed at improving the standards of integrity and transparency in executive local councils across Ukraine), willingness to cooperate with the project varies hugely across different municipalities. Many administrations are eager to learn from best practices in the area of transparent local governance, but others show no interest and refuse to cooperate, most likely because the full implementation of such standards might threaten vested interests within the local elite<sup>118</sup>. The disparity between national law on anti-corruption issues and local practice by state agents is reflected time and time again in the pages of the Business Ombudsman's reports<sup>119</sup>, leading the BOC to comment in their 2017 report on issues regarding local government and business that *"there is a clear trend towards more cases of abuse of office and exceeding authority by officials at local councils and state administrations..."*<sup>120</sup>. Based on the qualitative and quantitative data that we have reviewed in this section, this remark is a sadly fitting summary of the enduring prevalence of decentralized agent predation amongst local authorities in Ukraine, five years after the Maidan.

---

<sup>117</sup> Ibid.

<sup>118</sup> Interview with Alina Kubenko, Representative of Transparency International Ukraine conducted by the author in Kyiv, November 2018

<sup>119</sup> See, for example, Case No. 2 (a conflict of interest in local council contradicting national legislation) and Case no. 8 (Kyiv City Council adopting legislation contrary to national law) in: Business Ombudsman of Ukraine, "Systemic Report: Challenges for Government and Business for Dealing with Local Government" (2015), *op. cit.* pgs. 26, 36

<sup>120</sup> Ibid, pg. 24

## Section 4. Raidership in Post-Maidan Ukraine: Decentralized Predation in the Extreme

If the family of PR threats to private enterprise in Ukraine that we have been looking at could be ranked in severity, beginning with the relatively light risk of “corruption” from state bodies and then moving on to the more aggravated forms of rent seeking and intimidation that we have examined, then the phenomenon of “raidership” stands at the extreme end of the spectrum. As such, in much of the literature and public discussion of the issue, raidership is treated as a distinct conceptual category – although not in Ukrainian law<sup>121</sup>. Raidership poses the most total devastating to property rights there is, since a firm owner who suffers from it experiences complete expropriation and sees the ownership of her property and assets transferred to someone else. Thus, whilst earlier we challenged the epistemic utility of Markus’ distinction between certain types of corruption/rent seeking threats as “threats to income rights” and others as “threats to ownership rights”, there can be little disputing the fact that raidership is *de facto* a “threat to ownership rights” and should be classified as such. This makes it a particularly critical manifestation, or sub-category of the phenomenon of agent predation which we are examining.

Defining raidership as a concept is tricky because it is so easily confused with hostile takeovers, and is often misleadingly invoked by debtors whose property is being lawfully repossessed. In their report on the subject, the Business Ombudsman Council of Ukraine defines the term as “*the seizure or misappropriation of assets and/or corporate rights of a legal entity using unlawful methods and means*”<sup>122</sup>. In a report on the issue for Transparency International Ukraine published in 2012, Zimmerer notes that the closest which Ukrainian legislation and officialdom comes to a definition, in the Budget Declaration for 2008 – “*disposal of the state-owned property and corporate rights other than following the privatization proceedings or illegal seizure of a company*” is inadequate, and the author himself identifies three ideal types, or gradations of the phenomenon. Firstly, there is “white” raidership, where shares in a company are rapidly bought up, its debt acquired, and changes subsequently made to management, all technically within the law, but frequently without the consent or knowledge of other major shareholders. “Gray” raider attacks, by contrast, involve effecting a change of ownership in a firm by bypassing standard judicial and bureaucratic procedure and employing “*illegal means to foster the*

---

<sup>121</sup> Business Ombudsman Council of Ukraine (BOCU), “Systemic Report: Combatting Raidership: Current State and Recommendations”, 2017, page 8 ([https://boi.org.ua/media/uploads/ii\\_2017\\_sytem\\_en\\_digital.pdf](https://boi.org.ua/media/uploads/ii_2017_sytem_en_digital.pdf))

<sup>122</sup> *Ibid.*

*processes of gaining licenses, permits, favourable court decision or treatment by authorities*<sup>123</sup> in order to establish the veneer of sound legal foundation for the expropriation. Lastly, “black” raidership occurs when sheer brute force and intimidation – most commonly through law enforcement agents but occasionally with the help of hired thugs – is exercised, accompanied by falsification and forgery of documents, to seize control over the physical space of the target company. Since the category of “white raidership” is more or less indistinguishable from aggressive (but legal) takeovers, a common phenomenon in most market economies, we shall follow Markus (2015) and most other authors on the subject in concerning ourselves only with “gray” and “black” raidership, which are most closely bound up with the frailties of property rights security in Ukraine.

“Raidership” is often used synonymously with “predation” in reference to the seizure of private property through dubious application of legal powers, or the abuse of legal procedure, since many of the techniques used by “agent predators” already discussed frequently come hand in hand with complete expropriation of property – for example, when a business owner enlists the services of his allies in local law enforcement agencies to conduct a sham “investigation” into the operations of a rival business, and in the process seize possession of the rival enterprises assets after they have been confiscated or their ownership rights transferred during the investigation and judicial process. Thus, raidership in modern Ukraine is chiefly carried out through technically albeit superficially legal channels and with the connivance of courts or the state’s administrative apparatus. This is a significant change from the years immediately following the collapse of the Soviet Union, when the disintegration of organized state authority in many of the former soviet republics such as Ukraine and the uncertain state of property rights allocation led to widescale forceable expropriation of property by ruthless businessmen and criminal gangs with the enlistment of their own private enforcers. In most transition countries today, including Ukraine, the main source of raidership threats are not lawless criminal gangs or privateers, but state bureaucrats employing their administrative powers to advance their own and/or their commercial partners’ interests at the expense of private firms.

### “Centralized” Raidership in the Yanukovych Era

Given our interest in small-scale but economically devastating agent predation on the local bureaucratic level, the question that arises is: how decentralized is the practice of raidership in Ukraine? By which we mean, to what extent is raidership or outright expropriation of private property not monopolized as

---

<sup>123</sup> Gábor Zimmerer, “Raider Attacks in Ukraine”, *Transparency International Ukraine*, 2012 ([https://ti-ukraine.org/wp-content/uploads/2016/12/raider\\_attacks\\_-\\_ti\\_ukraine\\_eng.pdf](https://ti-ukraine.org/wp-content/uploads/2016/12/raider_attacks_-_ti_ukraine_eng.pdf)), accessed July 2019

the sole preserve of the state principal, as so much of the theoretical literature assumes? One way that we can begin to answer this question is by considering how the wider political context and the constraints (or lack thereof) imposed upon the state principal have historically influenced the situation on the ground: is there evidence to suggest that a more restrained state principal or central power which commits to upholding property rights is able to impose these restraints successfully on lower level, local state agents? One of the findings of Markus (2015)'s research was that, contrary to much of the theoretical literature and common-sense expectations, commitments to property rights and anti-raidership policies made at the central state level do not necessarily translate into equally binding commitments further down along the administrative state and bureaucratic hierarchy, and in some cases can even exacerbate the predatory instincts of lower-level bureaucrats on the local level – this is what seems to have happened in the years following Ukraine's Orange Revolution in 2004, when established hierarchical networks binding central and local state agents (often referred to as "the power vertical") broke down and, freed from previous constraints and the threat of being held accountable by executive authority, predatory bureaucrats across the country ran riot against the rights of entrepreneurs<sup>124</sup>. The transition from the Yanukovich presidency to Ukraine's post-Maidan administration, which in many respects parallels the transition from Kuchma to Yushchenko and post-Orange Revolution Ukraine, can provide us with another test case to examine this idea.

During the Yanukovich presidency (2010 – 2014), Ukraine's system of governance was, by almost every relevant international metric, characteristically autocratic and constructed around a tightly controlled power vertical, with the Yanukovich clan at the top distributing monopolies in different areas of the economy to oligarchic allies as well as rents to subordinates further down the hierarchy. Constitutional constraints on the presidency had been weakened, and power was concentrated in the principal's family and his industrialist allies in the east of the country. Of course, at the same time, the Yanukovich clan did not possess a monopoly on raidership by state agents from a number of different agencies, who took advantage of gaps and ambiguities in Ukrainian legislation, inconsistent regulation of the business sector, and generally a "high level of lawlessness in public administration" to target firms. Raidership was recognized as an acute problem afflicting the rights of business owners; in his 2012 report for Transparency International, Gábor Zimmerer commented that "*The 'reyderstvo' phenomenon appears to be one of the major obstacles for effective business activity in Ukraine*"<sup>125</sup>. Nevertheless, as we have already seen from our earlier analysis of the changing characteristics of predation in the state fiscal service through successive governments and regime types in Ukraine, the scale of theft involved in any particular type of predation, corruption or rent-seeking and the extent to which it is centralized

---

<sup>124</sup> Markus (2015), pg. 157

<sup>125</sup> Zimmerer (2012), *op. cit.* pg. 8

by the state principal can be shaped significantly by the behaviour and power structure of each particular regime type.

As far as raiding is concerned, under Yanukovich the prevailing perception among commentators and Ukraine analysts was that, much like the systematic siphoning of the tax administration perpetrated in the interests of the Yanukovich clan, the most egregious examples were committed by the president himself and members of his circle. Although it would be going too far to say that the state principal was monopolizing raidership, without doubt a much greater proportion of the raids, particularly of large companies, that were conducted now took place under the auspices of the president's administration, and according to some accounts it became increasingly common for Party of Regions officials, locked out of the more lucrative rents and spoils awarded to members of the president's inner circle, to resort to raiding as their share of the proceeds from belonging to the Yanukovich "power vertical"<sup>126</sup>. After consolidating his clan's hold over law enforcement agencies and all major executive state bodies, Yanukovich was able to orchestrate raiding attacks on a grand scale against countless firms, with the main beneficiaries of these attacks typically being shadowy entities owned by members of the president's family or associates. The qualitative shift in the raidership landscape marked by Yanukovich's coming to power was noted by the chairman of the NGO "Anti-Raider Movement", Yuriy Kravets, who reported that "*While until [sic] 2010, 99 percent of major raider attacks were performed by court decisions, after the election of Viktor Yanukovich as president of Ukraine, the pressure comes through the law enforcement agencies*"<sup>127</sup>. Law enforcement agencies are of course frequently enlisted as instruments of rent and bribe extraction from firms, as documented endlessly in the above sections, but the change of locus of raiding activity from court decision to law enforcement agencies precipitated by the advent of Yanukovich is striking and calls for comment. The greater role attributed to law enforcement agencies in raidership attacks from 2010 suggests that the practice was increasingly becoming reserved for those state officials or patrons who were locked into the presidential power vertical; whereas bribing a judge to issue a court order declaring a change of ownership for a firm is a relatively straightforward and affordable investment for an unscrupulous official, the resources required to orchestrate a criminal investigation into the firm which would bring the tax administration service and the public prosecutor into action at the service of the raider are considerably greater, and would demand a level of political influence that could only be sanctioned and guaranteed by the president's own patronage network.

---

<sup>126</sup> Matthew A. Rojansky, "Corporate Raiding in Ukraine: Causes, Methods and Consequences", *Demokratizatsiya: The Journal of Post-Soviet Democratization*, Volume 22, Number 3 / Summer 2014, pg. 423

<sup>127</sup> Quoted in Zimmerer (2012), op. cit. pg. 3

Even the country's most powerful oligarchs were kept in check by the threat of expropriation from the centre, which was great enough for them to desire an Association Agreement with the European Union in order to secure legal protection against raiding directed by the president's men<sup>128</sup>. Tellingly, one of the most notorious raiders in Ukraine, the oligarch Ihor Kolomoisky, who had built up his business empire through corporate raids in the 2000s (including "a literal raid on the Kremenchuk steel plant in 2006, in which hundreds of hired rowdies armed with baseball bats, iron bars, gas and rubber bullet pistols and chainsaws forcibly took over the plant..."<sup>129</sup>), was forced to cut down on his raidership after clashing with the new Yanukovich administration in 2010<sup>130</sup> - Kolomoisky was not in the president's good books, having backed his political rivals in the past<sup>131</sup>. The implication of this is that, when it came to high-value raiding, there was only one gang in town – the Yanukovich power vertical (or, in Hale's parlance, "patronage network"), which even the country's most influential oligarchs were unable to challenge.

A report from the Ukrainian newspaper *Dzerkalo Tyzhnia*, reacting to the latest wave of seizures of private companies orchestrated by the Yanukovich family in 2012, gives us a vivid picture of the mood of the business community and observers in the midst of the Yanukovich era, and how large the threat of expropriation from the state principal and his network of associates and underlings loomed in the perception of Ukraine's entrepreneurs. The report described what was happening in the country as a *Черговий тотальний переділ власності у виконанні нинішньої влади*, "yet another total redistribution of property, carried out by the current authorities" which "the family" [referring, very much in the mafia sense, both to the president's family members, in particular his son<sup>132</sup>, as well as Party of Regions allies] has obviously decided to take charge of", facilitated by their control over key ministries such as the Ministry of Internal Affairs and the Tax Administration, where confidants of Viktor and Oleksander Yanukovich (his eldest son) had taken senior positions<sup>133</sup>. The author compares

---

<sup>128</sup> Anders Åslund, "Ukraine crisis: Yanukovich and the tycoons", BBC News, 11.12.2013 (<https://www.bbc.co.uk/news/world-europe-25323964>), accessed July 2019

<sup>129</sup> Melik Kaylan, "An Injection of Rule of Law for Ukrainian Business? Oligarch's Lawsuit Could Help Improve The Culture Of Business Dealings In The Post-Soviet Space", *Forbes*, 15.07.2013 (<https://www.forbes.com/sites/melikkaylan/2013/07/15/an-injection-of-rule-of-law-for-ukrainian-business-oligarchs-lawsuit-could-help-improve-the-culture-of-business-dealings-in-the-post-soviet-space/#6da183f04ebe>), accessed July 2019

<sup>130</sup> Rojansky (2014), *op. cit.* pg. 425

<sup>131</sup> Interview with Ihor Kolomoisky, *Журнал "Предприниматель" ("Entrepreneur" Journal)*, 23.12.2010 (<http://predprinimatel.co.ua/en/kolomoyskiy-yanukovich.html>), accessed July 2019

<sup>132</sup> Who became one of the richest men in Ukraine during his father's presidency – see, for example, Ania Tsoukanova, "President's Millionaire Son Doubles Wealth on Ukraine Rich List." *Daily Monitor*, 31.03. 2013. (<http://www.monitor.co.ug/News/National/Presidents-millionaire-son-doubles-wealth-on-Ukraine-rich-list/688334-1735294-4vpqm4z/index.html>)

<sup>133</sup> Yuliya Mostova, *Perpetuum Peredelum*, *Dzerkalo Tyzhnia*, 20.01.2012 <https://dt.ua/POLITICS/perpetuum-peredelum.html> (Accessed January 2019)

Yanukovych to Ukraine's infamous former prime minister Pavel Lazarenko, imagining him declaring *"I will begin to share when everything becomes mine"* (*"Я почну ділитися тоді, коли все стане моїм"*), his priority being "the capture of the entire country".

From this 2012 analysis it becomes clear that the main beneficiaries of large-scale raiding in Ukraine in the years 2010 – 2014 were members of the Yanukovych clan, who used their senior positions in the central state apparatus and their control over law enforcement agencies to acquire *ЕКОНОМІЧНИХ ОБ'ЄКТІВ, ЯКІ СТАНОВЛЯТЬ ІНТЕРЕС* ("economic objects of interest") from political and business rivals. This is in keeping with the general characterization by international academic commentators on Ukraine of the Yanukovych years, a president who, as Åslund puts it, *"stands out for having driven public-asset theft to a new level and for having concentrated so much of the loot in his own hands and those of... the Yanukovych 'family.'..."*<sup>134</sup> by means of, among other schemes, the forced sale of private assets to the Yanukovych clan in acts of blatant corporate raiding<sup>135</sup>. In a report on corporate raiding in Ukraine for the Kennan institute which drew on numerous interviews with Ukrainian officials and business representatives, Matthew A. Rojansky hypothesized that the spate of raids which broke out during Yanukovych's presidency represented *"a new large-scale realignment of business ownership...in which those closest to Yanukovych were systematically stripping lucrative assets away from their previous owners, and they were doing so by means of corporate raids..."*<sup>136</sup>. Crucially, the very administrative and institutional instruments which were employed to seal to transfer of ownership of assets from legitimate owners to the raiders were designed in such a way that access to them was restricted as far as possible to the executive authorities; for example, in 2013, as part of government reforms aimed at "mitigating" raiding, the functions of the Ukrainian State Registry System (which is supposed to keep a record of the ownership rights held by individuals and corporate entities over immovable property) were centralized and brought under the control of the Ministry of Justice<sup>137</sup>. In a separate analysis of the raidership phenomenon, Michał Kozak describes how systematized corruption of the state registry system was, and integrated into the sinews of patronage of the Yanukovych power vertical; bribes paid to the clerks from the State Registry System *"ultimately landed in the pockets of people from the Yanukovych team"*, and an entire parallel economy developed around the practice, with the state principal extracting a fee for each transaction – *"A semi-official tariff of such bribes was calculated*

---

<sup>134</sup> Anders Åslund, "Oligarchs, Corruption and European Integration", *Journal of Democracy*, July 2014, Volume 25, No. 3, page 65

<sup>135</sup> Ibid, pg. 66

<sup>136</sup> Rojansky (2014), *op. cit.* pg. 423

<sup>137</sup> Michał Kozak, "'Raiding' in Ukraine in the 21st century is doing well again", Central European Financial Observer, 14.12.2016 (<https://financialobserver.eu/cse-and-cis/ukraine/raiding-in-ukraine-in-the-21st-century-is-doing-well-again/>), accessed July 2019

*depending on the size and location of the real estate*<sup>138</sup>. A parallel could be drawn here with the development of the state fiscal service during the Yanukovich era as a personalized instrument of rent extraction for the principal. Thus, it would not be much of an exaggeration to say that raidership, especially high-profile, large scale raidership, during this period of autocratic consolidation by the state principal was highly “centralized”, in the sense that a high proportion of raids were overseen by a chain of command ultimately leading to the presidential power vertical, whereas opportunities for more opportunistic raiding by bureaucrats and officials outside this power vertical, on the local level (for example, in municipal administrations), were restricted.

### Raidership in Post Maidan Ukraine: The Unabated Threat of Agent Predation

If raidership during the Yanukovich era was unusually centralized and it was the threat of expropriation by the state principal that loomed largest in the business community, then since the overthrow of the Yanukovich government in 2014 and the advent of successive administrations in 2014 and 2019 that have publicly declared themselves to be pursuing a reform-orientated, “European” direction for the country, the phenomenon of raidership has taken on a rather different aspect. Whilst the threat of outright expropriation from the president’s men has abated, there is plenty of evidence to suggest that raidership on the local level by unaccountable and decentralized officials and bureaucrats has proved resilient to reform efforts, and is even increasing.

The post-Maidan government took steps to tackle the country’s raidership problem by passing a series of legislative amendments in 2015, in particular “Law No. 815-VIII” and “Law No. 835-VIII”, which introduced a number of changes to the way in which state agencies and institutions processed applications for registering and altering ownership rights, including the following; more documentary evidence was required to edit the records on legal entities, the State Judicial Administration of Ukraine was required to provide evidence of court decisions referring to questions of registration and corporate rights, criminal liability was introduced for state registrars who were found to have broken the law in raidership cases, and a separate monitoring body was established under the Ministry of Justice for hearing complaints related to the State Registry<sup>139</sup>. Crucially, however, the entire process for registering (or transferring) property rights over immovable property and businesses was *decentralized*, resulting in, as the Business Ombudsman Council of Ukraine puts it “*demonopolization and decentralization of state registration of business and immovable property through liquidation of the former State*

---

<sup>138</sup> Michał Kozak, “‘Raiding’ in Ukraine in the 21st century is doing well again” (2016)

<sup>139</sup> BOCU, “Systemic Report: Combatting Raidership: Current State and Recommendations” (2017), *op. cit.* pg. 9

*Registration Service of Ukraine*<sup>140</sup>. Whereas under the previous system, every change made to the state registry was overseen by the Ministry of Justice, the new laws granted thousands of state notaries and registrars the power to register and amend rights over immovable property – furthermore, “*state registration of legal entities and physical persons-entrepreneurs were delegated to bodies of local self-governance, state administrations, notaries and entities, accredited by the Ministry of Justice of Ukraine.*”<sup>141</sup>

You can probably see where we are going with this. The centrifugal effects of the legislative amendments introduced by the Verkhovna Rada to combat raiding in 2015 evidently brought with them risks, since local actors not directly overseen by government ministries (including state notaries, registrars, and the local government bodies authorized to make changes to the state registry) effectively have greater discretion to make alterations in the official state records of company and property ownership, potentially for devious ends. The purpose of this raft of new legislation is perfectly reasonable and well intentioned; in a clear reaction to the abuses of the system under Yanukovich, the object was to avoid an over-centralized system with a market for bribes paid to the State Registration System and limited means of seeking redress for an unlawful action by the unaccountable bureaucrats sitting in the ministry. Yet what seems to have happened is that the opportunities opened up for local actors to manipulate the state registry has unleashed a new wave of more brazen and widespread raiding. In their systematic report on raidership, the Business Ombudsman Council explicitly notes that local authorities are more frequently playing a role in manipulation of the registration system, since their powers to assign postal addresses to property can be abused to divide up previously registered properties into different postal addresses registered under new owners, which “*provides raiders with a space for manoeuvres*”<sup>142</sup>. One of the cases recounted in the report illustrates the space for decentralized raiding that these powers have opened up; it concerns one of the state registrars of a village council in Kyiv Oblast, who was able to transfer ownership of a company from the legitimate director to someone else on the basis of forged documents<sup>143</sup>. Data released by Opendatobot, based on figures from General Prosecutor’s Office, indicate that the number of reported raidership attacks in Ukraine has been steadily rising over the past few years, surpassing 2013 levels in 2017:

---

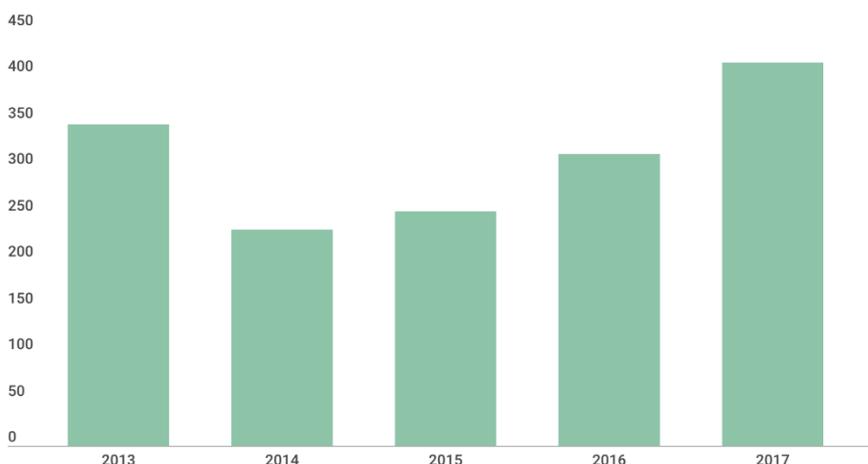
<sup>140</sup> BOCU, “Systemic Report: Combatting Raidership: Current State and Recommendations” (2017)

<sup>141</sup> Ibid

<sup>142</sup> Ibid, page 14

<sup>143</sup> Ibid, pg. 35

## Кількість рейдерських атак по рокам



"Number of Raider Attacks by Year", Source: Opendatabot: - [https://opendatabot.ua/blog/198-raiders?fbclid=IwAR2qKImhUeulnLq8SGv3dCLZpINZIIG\\_KjjWCTUeqbwNNkaOVthtqJYnSg8](https://opendatabot.ua/blog/198-raiders?fbclid=IwAR2qKImhUeulnLq8SGv3dCLZpINZIIG_KjjWCTUeqbwNNkaOVthtqJYnSg8)

The assessment of the rise of raidership attacks as an increasingly local problem is shared by Ivan Miroshnichenko, a Ukrainian MP and member of Business Varta, a civil organization that helps businesses to protect their property from raiders; he explains that in the past, most raidership attempts began with claims that violations were made during the privatization of a company, whereas now "in 30-40%" of cases, transfer of ownership is achieved through the forging of signatures and official documents "with the help of officials from local governments or the land registers"<sup>144</sup>. Oleksei Honcharuk, then writing in his capacity as head of Ukraine's Better Regulation Delivery Office (BRDO) – he has subsequently been appointed Prime Minister - also drew attention to the new wave of localized raiding that had been unleashed by the legislative changes mentioned above, arguing that "raider attacks have become easier and more primitive when the so called "authorized performers" were introduced at the legislative level"<sup>145</sup>.

Sadly, our analysis of decentralized agent predation in its purest form, raidership, has suggested that, far from being contained, the phenomenon is alive and kicking in contemporary Ukraine. Furthermore, it appears to have been exacerbated by legislative changes which have decentralized the process of

<sup>144</sup> Quoted in: Veronika Melkozerova, "Activists, Entrepreneurs and lawmakers unite to protect farm businesses from raiders", *Kyiv Post*, December 2017 (<https://www.kyivpost.com/business/activists-entrepreneurs-lawmakers-unite-protect-farm-businesses-raiders.html>), Accessed July 2019

<sup>145</sup> Oleksei Honcharuk, "It's time to stop hunting on business", *Better Regulation Delivery Office*, (<http://en.brdo.com.ua/analytics/s-time-stop-hunting-businesses/>)

registering and altering property rights, empowering local opportunistic state agents and heightening the risk of assaults on firms' property rights. This is yet another demonstration of how institutional constraints and credible commitments to property rights security made at the central state level are not necessarily replicated locally, and the decentralization of certain risk-bearing powers and responsibilities to local actors can have unintendedly destructive consequences.

## Conclusions

This research has attempted to explore the problem of decentralized agent predation in Ukraine by considering in turn, for the sake of analytical clarity, some of the main institutions and areas of the country's business environment through which it has been known to be practised; the tax administration system, state regulatory agencies, the regulatory role of local councils, and raidership. Unsurprisingly, the findings are complex and cannot be neatly distilled into straightforward conclusions. The prevalence of decentralized agent predation appears to vary across different sections of Ukraine's institutional structure and economy.

To begin with (Section 1), we found from semi-structured interviews that whilst predatory threats from the State Fiscal Service remain a large concern for Ukrainian businesses, reforms to the organizational structure of the tax administration system have contained and greatly reduced the localized rent-seeking and infringements against property rights that Markus (2015) described as endemic to tax administration on the local level in Ukraine. Instead, predation threats seem to be more concentrated at the oblast level, with larger companies more relatively affected than smaller, local firms. This is to some extent heartening, as it suggests that Ukraine's tax collection institutions have broken out of the cycle of industrial state principal-led predation followed by wholesale decentralized predation which characterized the transition from the Kuchma presidency to the Orange Revolution Period, and then to Yanukovich. In section 2, we examined the role of state regulatory agents and inspectorates in predation threats to Ukrainian firms, and found that, despite concerted efforts from the central government to contain the phenomenon, decentralized agents from a multitude of Ukraine's regulatory agencies still regularly abuse their discretionary powers to extract bribes, rents and even impinge on the property rights of firms. Nevertheless, judging from the Business Ombudsman's data, there is little evidence to suggest that predation is especially endemic to local agents from these agencies, as firms are just as likely to report abuses from the centre as from the periphery of these organizations.

Turning to the role of local councils and authorities in regulating the business environment, the evidence from a variety of business surveys as well as the semi-structured interviews yielded a worrying picture of the prevalence of decentralized agent predation at the local level in Ukraine, where the centrifugal tendencies of local elites and patron-client networks within local administrations have largely ignored or defied the reform commitments made at the central government level, by the state principal and parliament. These findings lend support to and serve as an empirical analogy to Markus (2015)'s contention, based on a study of post Orange Revolution Ukraine, that the "sovereign commitment" approach to securing property rights can all too easily be undermined by local decentralized agents. One important difference from the post Orange Revolution situation, however, seems to be that increasingly these local patrons and their allies prefer to establish and consolidate monopolies for their own companies and use their political and regulatory powers to suffocate their rivals and deny them a level playing field (for example, through the abuse of public tenders), rather than expropriating the assets of legitimate owners and extracting regular rents from them. The enduringly widespread practice of raidership in Ukraine, exacerbated by centrifugal legislative initiatives, further testifies to the persistence of the purest form of decentralized agent predation in Ukraine, and is a useful corrective the assumption that such problems can be solved by credible commitments to property rights and other enlightened reforms by the state principal.

## Bibliography

### English Language Materials

Acemoglu, Daron and Robinson, James A. - "Why Nations Fail: The Origins of Power, Prosperity and Poverty", New York: Crown Publishing Group, 2012

Allina-Pisano, Jessica – "The Post-Soviet Potemkin Village: Politics and Property Rights in the Black Earth". Cambridge University Press, 2007

American Chamber of Commerce in Ukraine - "Results of Chamber Corruption Perception Survey", 2017 ([http://publications.chamber.ua/2018/Chamber\\_CPS\\_2017.pdf](http://publications.chamber.ua/2018/Chamber_CPS_2017.pdf))

American Chamber of Commerce in Ukraine, "Meeting with Ms. Kseniya Lyapina, Head of the State Regulatory Service of Ukraine" (press release), 23.11.2015 (<http://chamber.ua/en/Events/Event/1460>)

Åslund, Anders - "Will Ukraine be able to Establish Real Property Rights?", mBank – CASE Seminar Proceedings No 153/2017, *Centre for Social and Economic Research*, 2017 ([https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3130127](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3130127)), EU4Business, "Investing in SMEs in the Eastern Partnership, Country Report: Ukraine", June 2018

Åslund, Anders – "Ukraine: What Went Wrong and How to Fix It", Peterson Institute for International Economics, 2015

Åslund, Anders - "How Ukraine became a Market Economy and a Democracy", Washington D.C., Peterson Institute (2009)

Åslund, Anders - "Ukraine crisis: Yanukovich and the tycoons", BBC News, 11.12.2013 (<https://www.bbc.co.uk/news/world-europe-25323964>)

Åslund, Anders - "Oligarchs, Corruption and European Integration", *Journal of Democracy*, July 2014, Volume 25, No. 3

Barzel, Yoram - "Economic Analysis of Property Rights", Cambridge: Cambridge University Press, 1997

Business Ombudsman Council of Ukraine: Quarterly Report, IV, 2019

([https://boi.org.ua/media/uploads/q42018/q4\\_2018\\_en.pdf](https://boi.org.ua/media/uploads/q42018/q4_2018_en.pdf))

Business Ombudsman Council of Ukraine: Annual Report 2018

([https://boi.org.ua/media/uploads/annual2018/annual\\_report\\_2018\\_en.pdf](https://boi.org.ua/media/uploads/annual2018/annual_report_2018_en.pdf))

Business Ombudsman Council of Ukraine: “Systemic Report: Challenges for Government and Business for Dealing with Local Government”, February 2017

([https://boi.org.ua/media/uploads/systemic\\_report\\_-\\_february\\_2017/system\\_01\\_en.pdf](https://boi.org.ua/media/uploads/systemic_report_-_february_2017/system_01_en.pdf))

Business Ombudsman Council of Ukraine, “Systemic Report: Combatting Raidership: Current State and Recommendations”, 2017

([https://boi.org.ua/media/uploads/ii\\_2017\\_sytem\\_en\\_digital.pdf](https://boi.org.ua/media/uploads/ii_2017_sytem_en_digital.pdf))

Denisova-Schmidt, Elena and Huber, Martin - “Regional Differences in Perceived Corruption among Ukrainian Firms”, Economics Working Paper Series 1407, University of St. Gallen, School of Economics and Political Science, April 2014 (<http://ux-tauri.unisg.ch/RePEc/usg/econwp/EWP-1407.pdf>)

Dubrovskiy, Vladimir - “The Political-Economic and Institutional Issues of The Ukrainian Tax System. Part III”, Vox Ukraine, 07.22.2015 ([https://voxukraine.org/en/the-political-economic-and-institutional-issues-of-the-ukrainian-tax-system\\_eng/](https://voxukraine.org/en/the-political-economic-and-institutional-issues-of-the-ukrainian-tax-system_eng/))

“EIDOS” Centre for Political Studies and Analysis, “Eidos”, 2016 Report

([http://eidos.org.ua/wp-content/uploads/2017/07/10%D1%80%D0%BE%D0%BA%D1%96%D0%B2\\_%D0%BE%D0%BD%D0%BB%D0%B0%D0%B9%D0%BD-%D0%B0%D0%BD%D0%B3%D0%BB.pdf](http://eidos.org.ua/wp-content/uploads/2017/07/10%D1%80%D0%BE%D0%BA%D1%96%D0%B2_%D0%BE%D0%BD%D0%BB%D0%B0%D0%B9%D0%BD-%D0%B0%D0%BD%D0%B3%D0%BB.pdf))

Fan, Simon, Lin, Chen, Treisman, Daniel - “Political decentralization and corruption: Evidence from around the world”, Journal of Public Economics, Volume 93, Issues 1–2, 2009, Pgs. 14-34

Hale, Henry - “Patronal Politics: Eurasian Regime Dynamics in Comparative Perspective”, Cambridge University Press, 2014

Hale and Orttung (eds) – “Beyond the Maidan: Comparative Perspectives on Advancing Reform in Ukraine”, Stanford University Press, 2016

Honcharuk, Oleksei - "It's time to stop hunting on business", Better Regulation Delivery Office, (<http://en.brdo.com.ua/analytics/s-time-stop-hunting-businesses/>)

Institute for Economic Research and Policy Consulting (IERP) - "Ukraine's Fight Against Corruption: The Economic Front", November 2018  
([http://www.ier.com.ua/files/publications/Policy\\_papers/IER/2018/Anticorruption\\_Report\\_EN.pdf](http://www.ier.com.ua/files/publications/Policy_papers/IER/2018/Anticorruption_Report_EN.pdf))

Kaylan, Melik - "An Injection of Rule of Law for Ukrainian Business? Oligarch's Lawsuit Could Help Improve the Culture Of Business Dealings In The Post-Soviet Space", Forbes, 15.07.2013  
(<https://www.forbes.com/sites/melikkaylan/2013/07/15/an-injection-of-rule-of-law-for-ukrainian-business-oligarchs-lawsuit-could-help-improve-the-culture-of-business-dealings-in-the-post-soviet-space/#6da183f04ebe>)

Kozak, Michał - "'Raiding' in Ukraine in the 21st century is doing well again", Central European Financial Observer, 14.12.2016 (<https://financialobserver.eu/cse-and-cis/ukraine/raiding-in-ukraine-in-the-21st-century-is-doing-well-again/>)

Lough, John and Dubrovskiy, Vladimir - "Are Ukraine's Anti-Corruption Reforms Working?", Chatham House Research Paper (2018), (<https://reader.chathamhouse.org/are-ukraines-anti-corruption-reforms-working#>)

Markus, Stanislav - "Property, Predation and Protection: Piranha Capitalism in Russia and Ukraine", Cambridge University Press, 2015

Levi, Margaret - "The Predatory Theory of Rule", *Politics and Society* 10, no. 4 (1981)

Levitas, Tony and Djikic, J. "Fiscal Decentralization and Local Government Finance Reform: 2014-2017", SKL/SIDA Policy Brief, 2018  
([https://www.academia.edu/37642724/Fiscal\\_Decentralization\\_and\\_Local\\_Government\\_Finance\\_Reform\\_In\\_Ukraine\\_2014-17](https://www.academia.edu/37642724/Fiscal_Decentralization_and_Local_Government_Finance_Reform_In_Ukraine_2014-17))

Libman, Alexander - "Democracy, size of bureaucracy, and economic growth: evidence from Russian regions", *Empirical Economics*, December 2012, Volume 43, Issue 3, pp 1321–1352,

Malolitneva, Vesta - "Reduction of Regulatory Burden on Small and Medium Enterprises: European Experience", VoxUkraine, 23.11.2015 (<https://voxukraine.org/en/reduction-of-regulatory-burden-on-small-and-medium-enterprises-european-experience/>)

Melkozerova, Veronika - "Activists, Entrepreneurs and lawmakers unite to protect farm businesses from raiders", Kyiv Post, December 2017 (<https://www.kyivpost.com/business/activists-entrepreneurs-lawmakers-unite-protect-farm-businesses-raiders.html>)

Mishra, Ajit - "Corruption, hierarchies and bureaucratic structure" in "The International Handbook on the Economics of Corruption", (Ed. Susan Rose-Ackerman), Edward Elgar Publishing, 2016

North, Douglass and Weingast, Barry - "Constitutions and Commitment: The Evolution of Institutions Governing Public Choice in Seventeenth-Century England", *The Journal of Economic History* 49, no. 4 (1989) pg. 803-32

OSCE - "Maintaining the Momentum of Decentralization in Ukraine", OSCE Multi Level Governance Studies, 2018 ([https://read.oecd-ilibrary.org/urban-rural-and-regional-development/maintaining-the-momentum-of-decentralisation-in-ukraine\\_9789264301436-en#page1](https://read.oecd-ilibrary.org/urban-rural-and-regional-development/maintaining-the-momentum-of-decentralisation-in-ukraine_9789264301436-en#page1))

Olson, Mancur "Dictatorship, Democracy and Development", *The American Political Science Review*, Vol. 87, No. 3 (Sep., 1993), pp. 567-576

PONARS Eurasia - "Ukraine in the Poroshenko Era: The Politics of Power, Reform and War", PONARS Eurasia Policy Perspectives, September 2017 ([http://www.ponarseurasia.org/sites/default/files/policy-perspectives-pdf/Ukraine%20in%20the%20Poroshenko%20Era\\_Ebook2017.pdf](http://www.ponarseurasia.org/sites/default/files/policy-perspectives-pdf/Ukraine%20in%20the%20Poroshenko%20Era_Ebook2017.pdf))

Rojansky, Matthew - "Corporate Raiding in Ukraine: Causes, Methods and Consequences", *Demokratizatsiya: The Journal of Post-Soviet Democratization*, Volume 22, Number 3 / Summer 2014

Rose-Ackerman, Susan "Corruption: A Study in Political Economy", New York: Academic Press, 1978

Rose-Ackerman, Susan (Ed.) - "The International Handbook on the Economics of Corruption", Elgar Publishing, 2016

Rudenko, Sehiy - "Mykola Azarov: Yanukovych's Right Hand Man", RFERL, 12.03.2010 ([https://www.rferl.org/a/Mykola\\_Azarov\\_Yanukovychs\\_RightHand\\_Man\\_/1982331.html](https://www.rferl.org/a/Mykola_Azarov_Yanukovychs_RightHand_Man_/1982331.html))

State Regulatory Service of Ukraine, "Partnering with the businesses towards building effective economic policy", 13.04.2017 ([http://www.drs.gov.ua/press-room/state-regulatory-service-ukraine-partnering-businesses-towards-building-effective-economic-policy/?print\\_page=true](http://www.drs.gov.ua/press-room/state-regulatory-service-ukraine-partnering-businesses-towards-building-effective-economic-policy/?print_page=true))

Stecklow, Steve, Piper, Elizabeth and Akymenko, Oleksandr - "Here's How Scams and Shakedowns Brought Ukraine's Economy to Its Knees", Reuters, 07.08.2014 (<https://www.businessinsider.com/r-special-report-how-scams-and-shakedowns-brought-down-ukraine-to-its-knees-2014-07?r=US&IR=T>)

Transparency International Ukraine - "Analytical Report: Ways to Ensure Investment Sector Transparency in Cities", August 2018, ([https://ti-ukraine.org/wp-content/uploads/2018/11/Analychnyj-zvit-pro-investysijnu-sferu\\_web\\_eng.pdf](https://ti-ukraine.org/wp-content/uploads/2018/11/Analychnyj-zvit-pro-investysijnu-sferu_web_eng.pdf))

Tsoukanova, Ania - "President's Millionaire Son Doubles Wealth on Ukraine Rich List." Daily Monitor, 31.03. 2013. (<http://www.monitor.co.ug/News/National/Presidents-millionaire-son-doubles-wealth-on-Ukraine-rich-list/688334-1735294-4vpqm4z/index.html>)

Umland, Andreas - The International Effects of Decentralization, Vox Ukraine, 30.1.2019 (<https://voxukraine.org/en/international-implications-of-ukraine-s-decentralization/>)

UNDP, Integrity and Inclusiveness of the Democratic Process in Ukraine - Analysis of Interim Research, Findings in the Regions, 2019, ([https://www.undp.org/content/dam/ukraine/docs/DG/Integrity%20and%20Inclusiveness%20Report%20FINAL\\_12%2003%202019.pdf](https://www.undp.org/content/dam/ukraine/docs/DG/Integrity%20and%20Inclusiveness%20Report%20FINAL_12%2003%202019.pdf)>.)

UNDP Ukraine, "Open Odesa: Keeping Track of City Decisions", 13.06.2019 (<https://undpukraine.exposure.co/open-odesa-keeping-track-of-city-decisions>)

World Bank - "Ukraine: Country Economic Memorandum: Strategic Choices to Accelerate and Sustain Growth", 31.08.2010,

(<http://documents.worldbank.org/curated/en/200401468314067900/pdf/558950ESW0UAOp1Official0use0only191.pdf>)

Zimmerer, Gábor - "Raider Attacks in Ukraine", Transparency International Ukraine, 2012

([https://ti-ukraine.org/wp-content/uploads/2016/12/raider\\_attacks\\_-\\_ti\\_ukraine\\_eng.pdf](https://ti-ukraine.org/wp-content/uploads/2016/12/raider_attacks_-_ti_ukraine_eng.pdf))

### Ukrainian Language Materials

Mostova, Yuliya – "Perpetuum Peredelum", Dzerkalo Tyzhnia, 20.01.2012

(<https://dt.ua/POLITICS/perpetuum-peredelum.html>)

Opendatabot – "З 2014 року кількість рейдерських захоплень зростає щороку" (since 2014 the number of raider attacks has increased every year), 02.07.2018

([https://opendatabot.ua/blog/198-raiders?fbclid=IwAR2gKImhUeulnLg8SGv3dCLZpINZIIG\\_KjWCTUeqbwNNka0VtqtqJYnSg8](https://opendatabot.ua/blog/198-raiders?fbclid=IwAR2gKImhUeulnLg8SGv3dCLZpINZIIG_KjWCTUeqbwNNka0VtqtqJYnSg8))

State Regulatory Service of Ukraine, "Аналітичний звіт ДРС за 2018 рік" (Analytical Report of the SRS for the year 2018), February 2019 (<http://www.drs.gov.ua/press-room/analichnyi-zvit-drs-za-2018-rik-2/>)

USAID - Щорічна оцінка ділового клімату (ABCA, Annual Business Climate Assessment),

USAID Leadership in Economic Governance Programme, 2017

(<https://www.slideshare.net/USAIDLEV/2016-2017-abcareportshort23042017final>)

### Russian Language Materials

Interview with Ihor Kolomoisky, Журнал “Предприниматель” (“Entrepreneur” Journal),  
23.12.2010 (<http://predprinimatel.co.ua/en/kolomoyskiy-yanukovich.html>)

Lekh, Irina - “Три года с начала Запорожского Майдана: что изменилось?” (“Three years since the beginning of the Zaporizhian Maidan: what has changed?”), 30.10.2016  
(<http://irinaleh.com.ua/tri-goda-s-nachala-zaporozhskogo-maydana-cto-izmenilos>)

Shelyazhenko, Yuriy - “Гагаркин: "народный" налоговый Харьков или теневой "решала"”, *Korrespondent*, 11.06.2015  
(<https://blogs.korrespondent.net/blog/business/3526144/>)